

No. 17037

United States
Court of Appeals
for the Ninth Circuit

BUILDING SYNDICATE COMPANY, an Ore-
gon Corp.,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

Transcript of Record

Appeal from the United States District Court
for the District of Oregon.

FILED

OCT 12 1960

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

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For Appellee.

The United States District Court
for the District of Oregon

Civil No. 9887

BUILDING SYNDICATE CO., an Oregon Cor-
poration,

Plaintiff,

vs.

UNITED STATES OF AMERICA,

Defendant.

PRETRIAL ORDER

This cause came on regularly for pretrial conference before the undersigned judge of the above-entitled court on the 4th day of November, 1959. Plaintiff was represented by Thomas B. Stoel, George H. Fraser, and David Hayhurst, its attorneys, and defendant was represented by its attorneys.

Statement of Agreed Facts

The following matters are admitted as to the issues framed by the complaint herein and the answer of the defendant to said complaint, and may be considered as evidence for all purposes:

I.

Plaintiff brings this action to recover from defendant federal income taxes for the calendar year 1953, paid by plaintiff to the District Director of Internal Revenue, Portland, Oregon, and interest.

II.

Jurisdiction is based upon Section 1346, Title 28, United States Code.

III.

Plaintiff is a corporation organized and existing under the laws of the State of Oregon, with its principal place of business in Portland, Oregon.

IV.

In the spring of 1927, the real property then known as the Northwestern Bank Building property was owned by the Northwestern National Bank of Portland (Oregon), a national banking association. Prior to June 21, 1927, the Northwestern National Bank of Portland (Oregon) placed this property in the hands of George N. Black, a real estate broker, for purposes of sale. Also prior to June 21, 1927, George N. Black entered into negotiations with George W. York & Company, Inc., Cleveland, Ohio, relative to financing the sale of the property known as Northwestern Bank Building. These negotiations culminated in a commitment by George W. York & Company, Inc., dated June 21, 1927, as set forth in Pretrial Exhibit 1.

V.

Building Syndicate, an Oregon corporation, was organized on or about August 1, 1927. Copies of the articles of incorporation, the bylaws, and the minutes through page 48 are set forth in the minute book as Pretrial Exhibit 2.

VI.

Some time after June 21, 1927, George W. York & Company, Inc., associated with it The Union Trust Company of Cleveland for the purpose of carrying out its commitment. Pretrial Exhibit 3 is a copy of a prospectus published by The Union Trust Company.

VII.

By deed dated September 16, 1927, the Northwestern Bank Building property was conveyed by Northwestern National Bank, a national banking association, to Security Savings and Trust Company (Portland, Oregon). Pretrial Exhibit 4 is a copy of the deed of conveyance, and Pretrial Exhibit 5 is a copy of an assignment of lease on a small parcel of the property. Under date of August 15, 1927, though actually executed September 30, 1927, Security Savings and Trust Company as trustee and The Union Trust Company (of Cleveland, Ohio) as co-trustee, executed an Agreement and Declaration of Trust between themselves and "The Holders of Land Trust Certificates of Equitable Ownership in the Northwestern Building Site Located in Portland, Oregon, Leased to Building Syndicate (an Oregon corporation)." Pretrial Exhibit 6 is a copy of said Agreement and Declaration of Trust. A lease of the property was entered into between Building Syndicate as lessee and Security Savings and Trust Company, trustee, as lessor, the lease being made as of August 15, 1927, though actually signed September 30, 1927. Pretrial Ex-

hibit 7 is a copy of this lease. Building Syndicate entered into an indenture with Lumbermen's Trust Company made as of September 1, 1927, to secure an issue of \$750,000 first mortgage leasehold bonds. Pretrial Exhibit 8 is a copy of this indenture. Payment to the seller for the property and delivery of the above-described documents were effected in a single escrow transaction on September 30, 1927, pursuant to an escrow agreement entered into by Northwestern National Bank, Security Savings and Trust Company, Lumbermen's Trust Company, and Building Syndicate with Title and Trust Company as escrow agent. The escrow agreement has not been located.

VIII.

The Northwestern Bank Building property was conveyed to the trustee for the Land Trust Certificate holders upon payment to the seller of \$2,202,133.07. The sources of the funds for payment of the foregoing purchase price by the trustee were as follows:

From trustee for Land Trust Certificate holders (Proceeds of sale of 1,350 Land Trust Certificates of Equitable Ownership)	\$1,250,000.00
From Building Syndicate (Proceeds of sale of leasehold bonds and of stock)	952,133.07
	<hr/>
	\$2,202,133.07

IX.

The name of the property was changed to American Bank Building at the beginning of the year 1928. In 1932, the leasehold bonds of Building Syndicate went into default. A bondholders' committee was organized. In 1933, an amendment to the lease was negotiated with The Union Trust Company of Cleveland which reduced the annual rental from \$74,250 to \$40,500 plus all of the net earnings received by Building Syndicate from the American Bank Building property up to the amount of the rental required by the original lease, this arrangement to remain in effect for five years. Pretrial Exhibit 9. On the expiration of this lease modification in 1938, a modification for an additional five-year period was negotiated with representatives of The Union Trust Company of Cleveland. Pretrial Exhibit 10.

X.

In 1943, the leasehold bonds of Building Syndicate being still in default, the trustee for the bondholders, at December 31, 1943, acquired the company's assets. On November 9, 1944, a new corporation known as Building Syndicate Co. (plaintiff herein), was organized. The assets of Building Syndicate (old company), including its leasehold on the American Bank Building, were transferred to plaintiff on December 31, 1944, the acquisition of the assets by the trustee and their transfer to plaintiff being a tax-free reorganization under the Internal Revenue Code.

XI.

Article Four of the lease of August 15, 1927 (Pretrial Exhibit 7), granted plaintiff an option to purchase the fee interest in the American Bank Building property from the lessor, upon 60 days' notice, for \$1,417,500. Plaintiff exercised this option to purchase on October 31, 1945. The sources of payment of the aforementioned option prices were as follows:

Proceeds of loan to Building Syndicate Co. from Prudential Insurance Company	\$1,200,000
Application of 138 Land Trust Certificates held by trustee in depreciation fund pursuant to provisions of lease (at \$1,050 per certificate).....	144,900
Financed from corporate funds of Building Syndicate Co.....	72,600
	\$1,417,500

XII.

The total cost of the American Bank Building property was set up on plaintiff's books in the amount of \$1,842,023.14. This amount reflects the following adjustments to the option price of \$1,417,500:

Purchase price	\$1,417,500.00
Add:	
Expenses of purchase.....	4,441.77

Unamortized balance of leasehold estate per books as of December 31, 1944..	444,195.80
	<hr/>
	\$1,866,137.57
Less purchase discount on Land Trust Certificates held in depreciation fund \$	24,144.43
	<hr/>
Total cost of property per plaintiff's books	\$1,842,023.14

XIII.

Plaintiff allocated the foregoing total cost of the property as follows:

Land	\$ 817,027.29
Building, less Dunham System, elevators, and alterations	1,000,779.96
Dunham System, elevators, and alterations	19,591.33
Leasehold, Parcel B (unamortized)...	4,624.56
	<hr/>
	\$1,842,023.14

XIV.

On their federal income tax returns from 1927 through 1944, plaintiff and its predecessor each year claimed deductions on the American Bank Building on the basis of the remaining life of the building (assumed in 1927 to be 36 years) rather than amortizing the cost of the 99-year leasehold which they held. On its tax return for the year 1945, plaintiff claimed depreciation from January 1, 1945, on the new allocated cost of the building

shown in paragraph XIII based on an assumed life of 32 years from that date. For the ten months' period from January 1, 1945, to October 31, 1945, the depreciation so claimed amounted to \$26,061.92. Under these methods plaintiff and its predecessor had claimed deductions through October 31, 1945, in the aggregate amount of \$549,215.08. Computed on the basis of amortization over a 99-year life, the aggregate amortization of plaintiff's leasehold as of October 31, 1945, was \$172,272.65. The excess of the deductions taken over leasehold amortization was \$376,942.43, of which \$274,784.49 did not result in tax benefit.

XV.

The net basis to plaintiff at October 31, 1945, of the American Bank Building for purposes of depreciation will be as follows:

(1) If defendant is correct in its contentions:	\$ 544,184.92
(2) If plaintiff is correct in its contentions numbered 4 and 5.....	1,137,707.33
(3) If plaintiff is correct in its contention numbered 4 and incorrect in its contention numbered 5:.....	986,430.78

XVI.

A federal income tax return of the plaintiff for the calendar year 1953 was duly filed with the District Director of Internal Revenue, Portland, Oregon. At various dates in the year 1954, and on September 21, 1956, plaintiff made payments ag-

gregating \$133,487.32 as and for federal income tax for the calendar year 1953.

XVII.

On October 26, 1956, plaintiff filed with the District Director of Internal Revenue, Portland, Oregon, a claim for refund of overpayment of federal income tax for the calendar year 1953. Thereafter, on July 18, 1957, plaintiff filed an amended claim for refund of overpayment of federal income tax for the calendar year 1953. By a notification dated April 2, 1958, the District Director of Internal Revenue rejected plaintiff's claim for refund of federal income tax for the year 1953 and interest thereon, in the aggregate amount of \$23,669.38.

Issues to Be Determined

1. Should the amount paid by plaintiff in 1945 at the time of its exercise of its option to purchase the American Bank Building property be taken into account in computing plaintiff's basis for depreciation of the property?

2. Should plaintiff's basis for the American Bank Building be reduced by the amounts claimed by plaintiff and its predecessor on the American Bank Building in excess of amortization of its leasehold cost to the extent such excess resulted in no tax benefit?

Contentions

Plaintiff contends:

1. As a matter of law the trustee acquired for the benefit of the Land Trust Certificate holders

the entire legal and beneficial interest in the American Bank Building property in 1927, subject only to a leasehold and option to purchase in Building Syndicate.

2. As a matter of law Building Syndicate acquired in 1927 only the interest in the American Bank Building property granted it by the terms of the lease agreement, which is Pretrial Exhibit 7.

3. On October 1, 1945, plaintiff, as successor to the rights of Building Syndicate, exercised the option to purchase contained in the lease agreement. As a matter of law plaintiff thereby acquired the interest previously held by the trustee for the benefit of the Land Trust Certificate holders. Prior to this date, as a matter of law plaintiff and its predecessor held only the rights of a lessee in the property granted under the terms of the lease agreement.

4. The amount paid by plaintiff on exercise of its option to purchase from the trustee must be taken into account in the computation of plaintiff's basis for the American Bank Building property for tax purposes.

5. Amounts claimed by plaintiff and its predecessors as deductions on the American Bank Building in excess of amortization of its leasehold cost (to the extent such excess resulted in no tax benefit) should not be applied to reduce plaintiff's basis for the property for tax purposes.

Contentions of Defendant

1. Building Syndicate (old company) properly claimed ownership of the Northwestern (American) Bank Building for federal income tax purposes; legal title to the building was vested in Security Trust pursuant to a financial plan adopted by the parties in order to secure the funds advanced by the holders of the land trust certificates which Building Syndicate needed in order to exercise its option to purchase this property.

2. The closing agreement executed by Building Syndicate (old company) on February 26, 1929, and accepted by the Secretary of Treasury on or about May 24, 1929, bars Building Syndicate Co. (new company) from changing the basis upon which depreciation was claimed and allowed on the Northwestern (American) Bank Building.

3. Ownership of the Northwestern (American) Bank Building for federal income tax purposes is controlled by the substance of the series of interlocking transactions leading up to execution of the escrow agreement of September 30, 1927, and not by the form of the legal instruments or remedies of the parties as construed and applied by the laws of the forum state.

4. Building Syndicate Co. may not adjust its basis in the Northwestern (American) Bank Building under the so-called tax benefit rule, when it failed to apply this adjustment at the time and in the manner prescribed by law.

Pretrial Exhibits

The parties agree that no further identification of the following pretrial exhibits is necessary and that recording data shown with respect to any exhibit is accurate and may be considered as evidence for all purposes. In the event said exhibits, or any of them, are offered in evidence at the time of the trial, they shall be subject to objection only on the grounds of relevancy, competency, and materiality.

Plaintiff's Exhibits:

1. Letter of George W. York & Co., Inc., to Mr. Geo. N. Black and Strong & MacNaughton Trust Company, dated July 21, 1927.
2. Material set forth in first 48 pages of minute book of Building Syndicate.
3. Copy of prospectus published by The Union Trust Company of Cleveland relating to Land Trust Certificates.
4. Deed from Northwestern National Bank of Portland, Oregon, to Security Savings and Trust Company, recorded in the Deed Records of Multnomah County, Oregon, in Book 1120 at page 230.
5. Assignment of lease from Northwestern National Bank of Portland, Oregon, to Security Savings and Trust Company, recorded in the Deed Record of Multnomah County, Oregon, in Book 1120 at page 231.
6. Copy of Agreement and Declaration of Trust between Security Savings and Trust Company as

Trustee, The Union Trust Company as Co-trustee, and The Holders of Land Trust Certificates of Equitable Ownership in the Northwestern Building Site Located in Portland, Oregon, Leased to Building Syndicate, dated August 15, 1927, and recorded in the Deed Records of Multnomah County, Oregon, in Book 1120 at page 134.

7. Lease dated August 15, 1927, from Security Savings and Trust Company, Trustee, lessor, to Building Syndicate, lessee, recorded in the Deed Records of Multnomah County, Oregon, in Book 1123 at page 10.

8. Leasehold bond indenture between Building Syndicate and Lumbermen's Trust Company made as of September 1, 1927.

9. Supplemental indenture of lease between Security Savings & Trust Company and Building Syndicate made as of May 15, 1933, signed and delivered December 21, 1933.

10. Second supplemental indenture of lease from The First National Bank of Portland to Building Syndicate, dated as of May 15, 1938.

11. Deed from The First National Bank of Portland, trustee, to Building Syndicate Co., dated October 29, 1945, and recorded in the Deed Records of Multnomah County, Oregon, in Book 982 at page 294.

12. Assignment of lease from The First National Bank of Portland, trustee, to Building Syn-

dicate Co., dated October 29, 1945, and recorded in the Deed Records of Multnomah County, Oregon, in Book 982 at page 297.

13. Quitclaim deed from Building Syndicate to Building Syndicate Co., dated February 17, 1945, and recorded in the Deed Records of Multnomah County, Oregon, in Book 908 at page 54.

14. Quitclaim deed from The National City Bank of Cleveland, successor co-trustee, to Building Syndicate Co., recorded in the Deed Records of Multnomah County, Oregon, in Book 1001 at page 323.

15. Printed letter dated July 17, 1933, from Building Syndicate to Holders of Land Trust Certificates.

16. Printed letter dated July 22, 1938, from Building Syndicate to Holders of Land Trust Certificates.

17. Booklet issued by George W. York & Co., Inc., entitled "The Land Trust Certificate Analyzed for Investors."

18. Income bond indenture between Building Syndicate Co. and Portland Trust & Savings Bank, trustee, made as of January 1, 1944.

19. Memorandum of option made as of July 7, 1927, from the Northwestern National Bank of Portland (Oregon) to George N. Black.

20. Memorandum of extension of option made as of August 6, 1927, from the Northwestern Na-

tional Bank of Portland (Oregon) to George N. Black.

Defendant's Exhibits
Offered and Introduced at Trial

50 A through 50 S. Original federal income and excess profit tax returns filed by Building Syndicate for the years 1927 through 1946, inclusive.

51 A through 51 Y. Copies of federal income and excess profit tax returns filed by Building Syndicate for the years 1927 through 1946, inclusive.

52 A through 52 P. Annual report of audit made of the books of Building Syndicate by independent certified public accountants for the years 1927 through 1939, inclusive.

53. Exhibit marked but not offered as evidence.

54 A through 54 F. Ledger sheets taken from the General Journal & Ledger of Building Syndicate.

Defendant's Exhibits

Exhibit No. 50

Original Income Tax Returns for Building Syndicate.

50-A—Corporation Income Tax Return, Year 1927.

50-B—Corporation Income Tax Return, Year 1928.

50-C—Corporation Income Tax Return, Year 1929.

50-D—Corporation Income Tax Return, Year 1930.

50-E—Corporation Income Tax Return, Year 1931.

50-F—Corporation Income Tax Return, Year 1932.

50-G—Corporation Income and Excess-Profits Tax Return, Year 1933.

50-H-1—Corporation Income and Excess-Profits Tax Return, Year 1934.

50-H-2—Corporation Income and Excess-Profits Tax Return, Year 1935.

50-I—Corporation Income and Excess-Profits Tax Return, Year 1936.

50-J—Corporation Income and Excess-Profits Tax Return, Year 1937.

50-K—Corporation Income and Excess-Profits Tax Return, Year 1938.

50-L—Corporation Income and Excess-Profits Tax Return, Year 1939.

50-M—Corporation Income, Declared Value Excess-Profits, and Defense Tax Return, Year 1940.

50-N—Corporation Income and Declared Value Excess-Profits Tax Return, Year 1941.

50-O—Corporation Income and Declared Value Excess-Profits Tax Return, Year 1942.

50-P—Corporation Income and Declared Value Excess-Profits Tax Return, Year 1943 (Tentative return, original First page missing).

50-Q—Corporation Income and Declared Value Excess-Profits Tax Return, Year 1944.

50-R—Corporation Income and Declared Value Excess-Profits Tax Return, Year 1945.

50-S—Corporation Income Tax Return, Year 1946.

Exhibit No. 51

Taxpayer's Copies of Income Tax Returns.

51-A—Corporation Income Tax Return, Year 1927.

51-B—Corporation Income Tax Return, Year 1928.

51-C—Corporation Income Tax Return, Year 1929.

51-D—Corporation Income Tax Return, Year 1930.

51-T—Corporation Income Tax Return, Year 1927.

51-F—Corporation Income Tax Return, Year 1932.

51-G—Corporation Income and Excess-Profits Tax Return, Year 1933.

51-H—Corporation Income and Excess-Profits Tax Return, Year 1934.

51-I—Corporation Income and Excess-Profits Tax Return, Year 1935.

51-J—Corporation Income and Excess-Profits Tax Return, Year 1936.

51-K—Corporation Income and Excess-Profits Tax Return, Year 1937.

51-L—Corporation Income and Excess-Profits Tax Return, Year 1938.

51-M—Corporation Income and Excess-Profits Tax Return, Year 1939.

51-N—Corporation Income, Declared Value Excess-Profits and Defense Tax Return, Year 1940.

51-O—Corporation Income and Declared Value Excess-Profits Tax Return, Year 1941.

51-P—Corporation Income and Declared Value Excess-Profits Tax Return, Year 1942.

51-Q—Corporation Income and Declared Value Excess-Profits Tax Return, Year 1943 (Tentative only).

51-R—Corporation Excess-Profits Tax Return, Year 1943.

51-S—Corporation Income and Declared Value Excess-Profits Tax Return, Year 1943.

51-T—Corporation Income and Declared Value Excess-Profits Tax Return, Year 1944.

51-U—Corporation Income and Declared Value Excess-Profits Tax Return, Year 1941 (Tentative).

51-V—Corporation Excess-Profits Tax Return, Year 1944.

51-W—Corporation Excess-Profits Tax Return, Year 1944 (Tentative).

51-X—Corporation Excess-Profits Tax Return, Year 1945.

51-Y—Corporation Income Tax Return, Year 1946.

Exhibit No. 52

Annual Accounting Reports of Independent Auditors.

52-A—Report of Arch F. Tourtelotte, CPA, as at 9/30/27.

52-B—Report of Chaney, Wood & Co., CPA, Period 10/1/27 to 12/31/28.

52-C—Report of I. D. Wood & Co., Year ended 12/31/29.

52-D—Report of I. D. Wood & Co., Year ended 12/31/30.

52-E—Report of I. D. Wood & Co., Year ended 12/31/31.

52-F—Report of Peat, Marwick, Mitchell & Co., Year ended 12/31/32.

52-G—Report of Peat, Marwick, Mitchell & Co., Year ended 12/31/33.

52-H—Report of Peat, Marwick, Mitchell & Co., Year ended 12/31/34.

52-I—Report of Peat, Marwick, Mitchell & Co., Year ended 12/31/35.

52-J—Report of Peat, Marwick, Mitchell & Co., Year ended 12/31/36.

52-K—Report of Peat, Marwick, Mitchell & Co., Year ended 12/31/37.

52-L—Report of Peat, Marwick, Mitchell & Co., Year ended 12/31/37.

52-M—Report of Peat, Marwick, Mitchell & Co., 6 mos. ended June 1938(6/ /38).

52-N—Report of Peat, Marwick, Mitchell & Co., Year ended 12/31/38.

52-O—Report of Peat, Marwick, Mitchell & Co., Year ended 12/31/42.

52-P—Report of Peat, Marwick, Mitchell & Co., Year ended 12/31/39.

Exhibit No. 54

Selected Pages From General Journal and
Ledger of Building Syndicate.

54-A—Typed insert appearing between Pages 26 and 27 of the General Ledger, entitled: “Proposed Depreciation and amortizing entries” as per letter of authorization from President, dated Feb. 9, 1928.

54-B—Ledger—Real Estate Parcel A.

54-C—Ledger—Leasehold Parcel B.

54-D—Ledger—Building, American Bank.

54-E—Ledger—Sinking Fund, Land Trust Certificate.

54-F—Ledger sheet entitled, “Land Trust Certificates.”

54-G—Ledger Sheet entitled, “Purchase Option, Parcels A & B.”

54-H—Ledger Sheet entitled, “Lease Rental.”

54-I—General Journal, Pages 144-145, December, 1929.

Jury trial is waived by both parties.

It Is Hereby Ordered that the foregoing pretrial order shall not be amended except by the consent of the parties or to prevent manifest injustice and that the said pretrial order supersedes all pleadings; and

It Is Further Ordered that upon the trial of this cause no proof shall be required as to matters of fact hereinabove specifically admitted, but that other proof upon the issues of fact and law as hereinabove stated may be had.

Dated at Portland, Oregon, this 4th day of November, 1959.

/s/ JOHN F. KILKENNY,
District Judge.

Approved:

/s/ THOMAS B. STOEL,
Of Attorneys for Plaintiff.

/s/ H. L. BIGGS,
Of Attorneys for Defendant.

[Endorsed]: Filed November 4, 1959.

[Title of District Court and Cause.]

OPINION

January 15, 1960

Kilkenny, Judge:

This is an action by plaintiff to recover from defendant certain income taxes paid by plaintiff.

In 1927 certain real property in Portland, Oregon, was owned by Northwestern National Bank of Portland¹. Prior to June 21, 1927, Northwestern placed this property in the hands of a real estate broker for sale. Prior to that time, this broker had negotiated with George W. York & Company, Inc.,² of Cleveland, Ohio, relative to financing the sale of the property. These negotiations culminated in a com-

¹Herein called Northwestern.

²Herein called York.

mitment by York dated June 21, 1927. Building Syndicate³, an Oregon corporation, was organized on August 1, 1927. Subsequent to June 21, 1927, York associated with it the Union Trust Company of Cleveland⁴ for the purpose of carrying out its commitment. By deed dated September 16, 1927, Northwestern conveyed said property to Security Savings & Trust Company⁵ (Portland, Oregon). On September 30, 1927, Security and Union, as co-trustees, executed an agreement and declaration of trust between themselves and "the holders of land trust certificates of equitable ownership in the Northwestern building site located in Portland, Oregon, leased to Building Syndicate (an Oregon corporation)." On September 30, 1927, Security leased to Syndicate the property involved for a period of 99 years. As of September 21, 1927, Syndicate entered into an indenture with Lumberman's Trust Company⁶ to secure an issue of \$750,000 first leasehold bonds. Payment to the seller for the property and delivery of the above-described documents were effected in a single escrow transaction on September 30, 1927, pursuant to an escrow agreement entered into between Northwestern, Security, Lumberman's and Syndicate, with Title & Trust Company as escrow

³Herein called Syndicate.

⁴Herein called Union.

⁵Herein called Security.

⁶Herein called Lumberman's.

agent. The Northwestern property was conveyed to the trustees, Union and Security, for the benefit of the land trust certificate holders upon payment to the sellers of \$2,202,133.07, the sources of these funds being:

From trustee for Land Trust Certificate holders (proceeds of sale of 1,350 Land Trust Certificates of Equitable Ownership)	\$1,250,000.00
From Building Syndicate (proceeds of sale of leasehold bonds and of stock)	952,133.07
	<hr/>
	\$2,202,133.07

In 1928 the name of the property was changed to American Bank Building. In 1932 the leasehold bonds of Syndicate went into default and a bondholder's committee was organized. In 1943, the bonds being still in default, the trustee for the bondholders acquired the company's assets on December 31st of that year. On November 9, 1944, a new corporation known as Building Syndicate Co.,⁷ the plaintiff herein, was organized. The assets of Syndicate, including its lease on the bank property, were transferred to the new company on December 31, 1944, the acquisition of the assets by the trustee and their transfer to plaintiff being a tax free reorganization under the Internal Revenue Code. The lease contained an option to purchase the fee interest of the property from the lessor upon written notice. Plain-

⁷Herein called new company.

tiff (new company) exercised this option to purchase on October 31, 1945, the sources of payment of the aforementioned option price being as follows:

Proceeds of loan to Building Syndicate Co. from Prudential Insurance Company	\$1,200,000
Application of 138 Land Trust Certificates held by Trustee in depreciation fund pursuant to provisions of lease (at \$1,050 per certificate)	144,900
Financed from corporate funds of Building Syndicate Co.	72,600
	\$1,417,500

On their federal income tax returns from 1927 through 1944, the plaintiff and its predecessors claimed depreciation deductions on the bank building each year on the basis of the remaining life of the building,⁸ rather than amortizing the cost over the 99 year leasehold period. On its tax return for the year 1945, plaintiff claimed depreciation from January 1, 1945, on the new allocated cost of the building based on an assumed life of 32 years from that date. For the ten months' period from January 1, 1945, to October 31, 1945, the depreciation so claimed amounted to \$26,061.92. Under these methods plaintiff and its predecessor had claimed deductions through October 31, 1945, in the aggregate amount of \$549,215.08. Computed on the basis of amortization

⁸Assumed in 1927 to be 32 years.

over a 99-year life, the aggregate amortization of plaintiff's leasehold as of October 31, 1945, was \$172,272.65.

On the income tax returns filed by the new company, it adjusted the cost basis of the property by adding the amount paid to redeem the land trust certificates and claimed a deduction for depreciation computed on the basis of this adjustment. To the extent the deductions thus claimed represented an amount for depreciation already allowed or allowable to Syndicate (old company) in its prior income tax returns, the Commissioner of Internal Revenue disallowed the deduction and assessed a tax deficiency. It is this deficiency which the plaintiff attempts to recover in this case.

Simply stated, the issue in this case is: Whether Syndicate properly claimed and was allowed an income tax deduction for depreciation on the American Bank Building (formerly Northwestern Bank Building) during the years 1927 through 1943 computed on the basis of the total purchase price paid to the original vendors of the property. The answer to the question is solved by determining whether Syndicate, during such years, should be treated as the owner, for tax purposes, of the building in question.

The corporate income and excess profit tax returns of Syndicate show that it regarded itself as the owner of the building during the years in question and that it claimed and was allowed an annual

deduction for depreciation on the basis of such ownership. This method of reporting was used after examination and discussion by and with the Internal Revenue Service and most of the reports were filed after a final closing agreement was executed by Syndicate and the Revenue Service. These returns indicate that the amount received from the sale of the land trust certificates was regarded as a corporate liability of Syndicate and that the land and building were a corporate asset. The annual accounting reports of Syndicate consistently showed that it regarded itself as the owner of the bank building. These reports show the trust certificates as a corporate liability and one of these reports affirmatively stated that legal title was vested in the trustee merely as a method for financing the purchase of the building. Likewise, the minutes of the meetings of the stockholders and of the board of directors, and the financial records of Syndicate, very definitely show that it regarded itself as the owner of the bank building and that the land trust certificates were liabilities on which interest was paid and accrued. It is unnecessary to point to other documentary evidence which, with the above, conclusively shows that Syndicate regarded itself as the owner of this building.

The construction against interest, in a tax case, by a party to a contract is strong evidence of its meaning. *Natco Corporation vs. United States*, 3 Cir., 1956, 240 F. 2d 398, 403; *Cutting vs. Bryan*, 9 Cir., 1929, 30 F. 2d 754. Plaintiff urges that the

testimony of the witnesses at the time of the trial overcomes the action of Syndicate from 1927 through 1943, inclusive. The principal witnesses testified to an intention which would be directly opposed to the action taken by the directors of all interested groups. Furthermore, this testimony would be in direct conflict with what I consider a proper construction of the instruments signed by the respective parties. A witness' statement concerning intention does not weigh heavily against facts directly to the contrary. *Flynn vs. Crume*, 7 Cir., 1939, 101 F. 2d 661.

Aside from the documentary evidence above-mentioned, the lease itself and the declaration of trust show that all parties to the transaction regarded Syndicate, not the trustees, as the real owner of the building. We call your attention to the following: Article IV of the Declaration of Trust, provides, among other things, for a depreciation fund, over which Syndicate had complete control if it so desired. This fund was connected with the right of Syndicate to exercise the option so that the entire fund could be used by Syndicate at any time it desired. Syndicate could ask for a transfer at any time into this depreciation fund of all of the land trust certificates, upon payment of \$1,050.00 each. If such a thing would happen, the entire fee of the property would necessarily belong to Syndicate, in that there would be no other beneficiary of the trust. This trust agreement further provides that in the event of an exercise of the option given to Syнди-

cate under the lease, any and all amounts which were in the depreciation fund should be credited on the purchase price. The lease was for a period of 99 years, renewable forever. The rental was fixed at $5\frac{1}{2}\%$ of the principal amount advanced and remained so fixed, irrespective of future contingencies or change in the values of the real property. The lease provided that if the property was appropriated to public use, such appropriation constituted an election by the lessee to purchase the property and if the appropriation was only partial, that there would be no reduction or abatement in the amount of rent paid. The lessee insured the property and the lessee was to receive the difference between the insurance proceeds and the cost of restoration in the event of any casualty.

I am of the opinion that this case is controlled by the general principles announced in *Helvering, Commissioner, vs. Lazarus*, 308 U.S. 252. In that case, on documents and a state of facts quite similar to those above recited, the United States Supreme Court held that the transaction between the taxpayer and the trustee bank, in form a transfer of ownership with a lease back, was in truth and in fact a loan secured by the property involved and that the taxpayer should be treated as the owner of the property for all tax purposes, including depreciation. Counsel for plaintiff cite a good many cases on when the court should consider the transaction a mortgage, rather than a transfer of ownership. Such cases are not controlling under this

factual situation. The government is not contending that the transaction created a mortgage. Plaintiff relies on *City National Bank Bldg. Co. vs. Helvering*, D.C., 1938, 98 F. 2d 216; *The Akron Dry Goods Co. vs. Commissioner*, 18 T.C. 1143. Although counsel argue otherwise, I feel that the benefit of *City National* to plaintiff's position was destroyed by the decision of the Supreme Court in the *Lazarus* case. The Supreme Court, in its decision in *Lazarus*, calls attention to the fact that it granted certiorari by reason of the fact that a different result was reached in *City National* than in *Lazarus*. The Court then proceeded to affirm the decision of the Board of Tax Appeals in *Lazarus*. Therefore, I consider *Lazarus* to be the law on this case.

The Akron Dry Goods Co. vs. Commissioner, *supra*, is of no help to the plaintiff. As a matter of fact, the decision in *Akron* actually supports the position of defendant in this case. I quote from the Tax Court opinion:

“* * * In treating the transaction as a sale in July, 1928, resulting in a deductible loss the petitioner realized a substantial income tax benefit for the fiscal year 1929. Thereafter, the properties were not carried on petitioner's books as capital assets and thus were not taken into account in a question involving petitioner's insolvency in the subsequent taxable year 1936, hereinafter discussed.

“The record herein does not support a conclusion that the July, 1928, transaction cast in the form of a

sale, was, in equity, a mortgage as contended by petitioner. Furthermore, now to correct for the purpose of a climaxed tax deduction benefit in the taxable year 1945 an alleged mistake, but actually an inconsistent position, which resulted in the petitioner's election to take tax deduction benefit in the taxable year 1929—a year as to which any adjustment is barred by the statute of limitations—would be contrary to the established principle of not allowing a double tax benefit. *Robinson vs. Commissioner*, 181 F. 2d 17, affirming 12 T.C. 246. Cf. *Wheelock vs. Commissioner*, 77 F. 2d 474, affirming 28 B.T.A. 611."

Clearly, the decision in the Akron case is in full accord with the government's position in this court.

I hold that Syndicate was the owner of the bank building during the years in question. Counsel for defendant will prepare findings and judgment in conformity with this opinion.

[Endorsed]: Filed January 15, 1960.

[Title of District Court and Cause.]

FINDINGS OF FACT AND CONCLUSIONS OF LAW

Findings of Fact

1. This is an income tax case brought by Building Syndicate Company to recover taxes paid for the calendar year 1953 in the amount of \$23,669.38.

2. Building Syndicate Company maintains that they should be allowed to take additional depreciation deductions on certain real estate owned by them.

3. The real estate in question is a building, which in 1927 was owned by Northwestern National Bank of Portland. During the year 1927, Northwestern Bank offered this building for sale through a real estate broker. This broker, George N. Block, paid \$10,000 for an option to purchase this property for approximately \$2,200,000.

4. In order to facilitate the sale of the building, the real estate broker secured a financial commitment from an Eastern concern whereby they would underwrite an issue of land trust certificates in the amount of \$1,350,000.

5. Building Syndicate, an Oregon corporation, was organized on August 1, 1927, with an authorized capital of 7,500 shares of no par common stock. This stock was subscribed at \$40 per share or an aggregate of \$300,000. George N. Block transferred to Building Syndicate his option to purchase the bank property in payment of \$10,000 on his subscribed stock.

6. The directors of Building Syndicate negotiated a commitment with the Lumbermen's Trust Company to underwrite \$750,000 of leasehold bonds to be issued by Building Syndicate.

7. The directors of Building Syndicate agreed that the building here in question be held in trust

by Security Savings and Trust Company of Portland, and Union Trust Company of Cleveland, Ohio. The trustees were to issue a lease to the Building Syndicate. This lease provided for a term of 99 years renewable forever. The purchase of the building and the necessary agreements were approved at a special meeting of the board of directors of Building Syndicate on September 19, 1927. The minutes of the board of directors state:

“There was thereupon presented to the Board for consideration a form of escrow agreement, dated as of September 19, 1927, proposed to be executed by Northwestern National Bank, Security Savings and Trust Company, Building Syndicate, Lumbermen’s Trust Company and a local bank to be named hereafter (said bank when named to act as agent for Northwestern Mutual Life Insurance Company, holder of a present mortgage on the Northwestern Bank Building property), said escrow being directed to Title and Trust Company, and setting forth in detail the amounts of money to be paid by this company for the purchase of said Northwestern Bank Building property, and the amounts of money to be received by this company from the purchasers of the 1350 land trust certificates, the issue of which has been hereinbefore authorized, and to be received from Lumbermen Trust Company for the purchase of the \$750,000.00 par value first mortgage leasehold bonds of this company, a copy of said escrow agreement being hereinafter set forth as Exhibit ‘D’ to the minutes of this meeting.

“On motion duly made and seconded, it was unanimously

“Resolved, that the President of this company execute in the name of this company and as its act and deed said escrow agreement.

“Resolved Further, that the President and Secretary of this company be and they hereby are authorized and empowered to deliver to Title and Trust Company, as escrow holder, all of the instruments provided to be delivered to it under the terms of said escrow agreement.

“Resolved Further, that said officers be and they hereby are authorized and empowered to consummate all sales of securities, execute and deliver all documents, receive all considerations for the sale of securities, and make all payments to Northwestern National Bank provided to be made by the terms of said escrow, and to do and perform all other acts required to be done by this company in order to effect the purchase of said Northwestern Bank Building property in time and manner as is provided for by the terms and conditions of said declaration of trust, Exhibit ‘A,’ said lease, Exhibit ‘B,’ said mortgage, Exhibit ‘C’ and said escrow agreement, Exhibit ‘D.’

“There being no further business to be transacted, the meeting adjourned.”

8. The terms of the escrow agreement were executed about September 30, 1927. The board of directors of Building Syndicate changed the name of

the property from the Northwestern Bank Building to the American Bank Building in 1928.

9. The property was conveyed to the trustees, for the benefit of the land trust certificate holders upon payment to the sellers of \$2,202,133.07. The sources of these funds were:

From Trustee for Land Trust Certificate Holders (Proceeds of sale of 1,350 Land Trust Certificates of Equitable Ownership)	\$1,250,000.00
From Building Syndicate (Proceeds of leasehold bonds and stock)	952,133.07
	\$2,202,133.07

10. The corporate income tax returns filed by Building Syndicate stated that their business was as follows:

Years	Business
1928 through 1931	Owns and Operates Office Building
1932 through 1935	Building Ownership
1936 through 1942	Building Owner
1943	Operator of Office Building

11. Through all the years 1927-1943 the Building Syndicate claimed and was allowed a deduction for depreciation based on a useful life of 36 years and computed on entire cost of the building.

12. The financial statements of the Company, as furnished with the income tax returns for all years

1927-1943, listed this property as a corporate asset and the land trust certificates and leasehold bonds as corporate liabilities. The annual accounting reports, prepared by independent accountants, consistently showed that Building Syndicate regarded itself as the owner of the bank building.

13. In 1932 the leasehold bonds of Building Syndicate were in default and a bondholder's committee was organized. In 1943 the bonds were still in default and the trustee of the bondholders foreclosed on Building Syndicate on December 31, 1943.

14. On November 9, 1944, a new corporation known as Building Syndicate Company was organized. This corporation is the plaintiff in this action. All the assets, including the lease on the bank building, were transferred from the trustee of the bondholders to the new corporation on December 31, 1944. The acquisition of the assets by the trustee and their transfer to plaintiff were pursuant to a tax-free reorganization under the Internal Revenue Code.

15. The original lease issued to Building Syndicate contained an option in favor of Building Syndicate whereby they could purchase the fee title from the lessor upon written notice. The trust agreement with the trustee also contained the provisions for acquisition of the fee title by Building Syndicate.

16. Plaintiff, pursuant to the option paid the required sums to the trustee and acquired title to the

property on October 31, 1945. The funds for such purchase were derived as follows:

Proceeds of loan from Prudential Insurance Co. to Building Syndicate Co.	\$1,200,000.00
Application of 138 Land Trust Certificates held by Trustee in depreciation fund pursuant to provisions of lease (at \$1,050 per certificate)	144,900.00
From Building Syndicate Co. corporate funds	72,600.00
	\$1,417,500.00

17. Depreciation claimed by plaintiff's predecessor through October 31, 1945, amounted to \$549,215.08. If depreciation had been computed on the basis of a 99-year life the depreciation would only have amounted to \$172,272.65.

18. On retirement of the land trust certificates the new company made an adjustment to the basis of the building. The undepreciated balance of the building cost was added to the amount paid in retirement of the land trust certificates and the total was reallocated among the land and building.

19. The retirement of the land trust certificates was equivalent to refinancing a loan and had no effect on the basis of property owned by the company.

20. During the years 1927 through 1943, Building Syndicate, for income tax purposes, was the owner of the property in question. Building Syndicate properly computed the depreciation allowance for this property based on the total purchase price of the depreciable building.

21. The basis for depreciation in the new company is the same as it was in the old.

Conclusions of Law

1. The Court has jurisdiction of the parties and of the subject matter of this action.

2. That plaintiff has failed in its burden of proof to establish its contentions and that defendant is entitled to judgment in its favor dismissing the above cause with prejudice and with costs.

3. The lease itself and the declaration of trust show that all parties to the transaction regarded Building Syndicate, not the trustees, as the real owner of the building.

4. Building Syndicate was the owner of the bank building during the years in question.

Dated this 13th day of April, 1960.

/s/ JOHN F. KILKENNY,
District Judge.

[Endorsed]: Filed April 13, 1960.

United States District Court,
District of Oregon

Civil No. 9887

BUILDING SYNDICATE CO., an Oregon Corporation,

Plaintiff,

vs.

UNITED STATES OF AMERICA,

Defendant.

JUDGMENT

The Court having considered the evidence and the arguments of counsel and having entered its findings of fact and conclusions of law herein,

It Is Ordered that the above cause be and the same is hereby dismissed with prejudice and that the defendant have and recover its costs and disbursements from plaintiff in the sum of \$.

Dated this 14th day of April, 1960.

/s/ JOHN F. KILKENNY,
District Judge.

[Endorsed]: Filed April 14, 1960.

[Title of District Court and Cause.]

NOTICE OF APPEAL

To: United States of America, defendant, and
C. E. Luckey, United States Attorney for the
District of Oregon, its attorney:

Notice Is Hereby Given and Building Syndicate
Co., an Oregon corporation, plaintiff above named,
hereby appeals to the United States Court of Ap-
peals for the Ninth Circuit from each and every
part of that certain judgment in favor of defendant
entered herein on April 14, 1960, and from the
whole thereof.

Dated: May 13, 1960.

/s/ THOMAS B. STOEL,

HART, ROCKWOOD, DAVIES,
BIGGS AND STRAYER,
Of Attorneys for Plaintiff-
Appellant.

Service of copy acknowledged.

[Endorsed]: Filed May 13, 1960.

[Title of District Court and Cause.]

STATEMENT OF POINTS

The points upon which plaintiff-appellants in-
tends to rely on this appeal are as follows:

1. The court erred in stating Findings of Fact Nos. 2, 19, 20 and 21 as Findings of Fact, since they are actually conclusions of law.

2. The court erred in concluding that plaintiff's predecessor, Building Syndicate, was the owner of the building for income tax purposes during the years 1927 through 1943 and that it properly computed depreciation on the total purchase price of the building (Findings of Fact No. 20), since the 1927 transaction was not a mortgage loan (Opinion, page 7).

3. The court erred in concluding that the retirement of the land trust certificates was equivalent to refinancing a loan and had no effect on the basis of the property (Findings of Fact No. 19) and that plaintiff's basis for depreciation is the same as that of its predecessor (Findings of Fact No. 21), since the 1927 transaction did not create a mortgage loan (Opinion, page 7).

4. The court erred in concluding that the Lease and Declaration of Trust show that all parties regarded Building Syndicate as the owner of the building (Conclusions of Law No. 3), since those documents conclusively establish that its interest was a leasehold with an option to purchase.

5. The court erred in making Finding of Fact No. 21 that the basis for depreciation in Building Syndicate Co. was the same as it was in the former Building Syndicate.

6. The court erred in making Finding of Fact No. 18 that the undepreciated balance of the build-

ing cost, rather than the unamortized balance of the leasehold estate, was added to the amount paid in retirement of the land trust certificates.

7. The court erred in concluding that plaintiff's predecessor, Building Syndicate, was the owner of the building during the years in question (Conclusions of Law No. 4), since its only interest in the building was a leasehold with an option to purchase.

8. The court erred in concluding that this case is controlled by the decision in *Helvering v. F. & R. Lazarus & Co.*, 308 U. S. 252, 60 S. Ct. 209 (1939) (Opinion, pages 6 and 7).

9. The court erred in concluding that plaintiff failed in its burden of proof herein (Conclusion of Law No. 2).

10. The court erred in failing to hold as a matter of law that neither plaintiff nor its predecessor made any investment in the building itself prior to exercise of the option to purchase in 1945.

11. The court erred in concluding that the conduct of plaintiff's predecessor, Building Syndicate, constituted a construction of the lease and declaration of trust against its interest (Opinion, page 5).

/s/ CLEVELAND C. CORY,
Of Attorneys for Plaintiff.

Service of copy acknowledged.

[Endorsed]: Filed August 3, 1960.

[Title of District Court and Cause.]

STIPULATION AND ORDER FOR
TRANSMITTAL OF EXHIBITS

It Is Hereby Stipulated and Agreed by and between the attorneys for the respective parties that an order may be entered directing the clerk of this court to transmit all the original exhibits herein to the clerk of the United States Court of Appeals in San Francisco, California; and it is further

Stipulated and Agreed that the printing of the said original exhibits may be dispensed with and that the said original exhibits may be handed to the court at the time of the hearing of the said appeal.

/s/ CLEVELAND C. CORY,
Of Attorneys for Plaintiff.

/s/ EDWARD J. GEORGEFF,
Of Attorneys for Defendant.

It Is So Ordered this 4th day of August, 1960.

/s/ JOHN F. KILKENNY,
United States District Judge.

Presented by:

/s/ CLEVELAND C. CORY,
Of Attorneys for Plaintiff.

[Endorsed]: Filed August 4, 1960.

United States District Court
District of Oregon

Civil No. 9887

BUILDING SYNDICATE CO., an Oregon Corporation,

Plaintiff,

vs.

UNITED STATES OF AMERICA,

Defendant.

November 4, 1959

Before: Hon. John F. Kilkenny, District Judge.

Appearances:

MESSRS. THOMAS B. STOEL,
GEORGE H. FRASER, and
DAVID G. HAYHURST,
Of Attorneys for Plaintiff.

MESSRS. ARTHUR L. BIGGINS and
EDWARD J. GEORGEFF,
Assistants United States Attorney,
Appearing for Defendant.

TRANSCRIPT OF PROCEEDINGS

The Court: Are the parties ready in Building
Syndicate versus United States, Civil 9887?

Mr. Stoel: Ready for plaintiff.

Mr. Biggins: The Government is ready, your
Honor.

The Court: I take it the pretrial order has not been signed by Counsel. I will pass that to the bailiff, and we will have that signed before we proceed. Gentlemen, do you care to make opening statements? I have read your memorandums and the Agreed Facts but not the contentions in the pretrial order. I have not had time to read the contentions. You may use your own judgment as to whether you want to make the opening statements. Mr. Stoel?

Mr. Stoel: I would like to make a brief opening statement, your Honor.

The Court: Yes; you may proceed.

Mr. Stoel: Your Honor, the basis, the question in this case is the basis of depreciation of the American Bank Building owned by the plaintiff, and this question, we believe, turns on the nature of the transaction in 1927 by which the Northwestern Bank Building was sold.

For the convenience of your Honor, we have prepared a chart that appears on the blackboard there, trying to demonstrate the nature of the interests that were created in connection with the transaction in 1927 as we conceive them to be and the flow of money that occurred in order to accomplish the purpose. With your permission, I may from time to time refer to that as a means of illustrating my opening statement.

In 1927 what is now the American Bank Building property, then known as the Northwestern National Bank property, was for sale. A local real estate

broker named George Black was interested in trying to arrange a sale of the property. In connection with working out a plan for the sale, he learned of the financing [2*] device known as Land Trust Certificates, which had achieved some popularity in Ohio at this time, and he communicated with an Ohio underwriting firm, George W. York & Company, to learn how this device might be applied in developing an arrangement for the purchase of this building.

The communications with George W. York and Company by Mr. George Black resulted in a commitment letter from George W. York Company to Mr. Black, describing how the Land Trust Certificate device plus a leasehold might be used to acquire the property.

Mr. Black then obtained an option from the owners of the property to purchase it for cash for approximately two million, two hundred thousand dollars. I might say that these figures are rounded off here so that we will not be bothered with odd dollars or cents.

Mr. Black was still in the position of a commission agent attempting to arrange a way of selling this property, and he took his proposition to the local businessmen, including Mr. Harry Kendall, for help in working out the solution which George W. Black had proposed. That resulted in a local group of businessmen working up interest locally in furnishing the funds which would be required in addition to the sale of the Land Trust Certificate proceeds to purchase the property.

*Page numbering appearing at top of page of original Reporter's Transcript of Record.

The local businessmen determined that they could sell first mortgage leasehold bonds on this property in the amount of about [3] \$750,000, and they determined that they could raise locally or stock in a company to become lessee of the proposed company \$300,000, and in early August they formed a company known as Building syndicate with a capitalization of \$300,000 and with subscriptions for stock in that amount.

That company took an assignment from George Black, as shown by the dotted line coming down from Building Syndicate (indicating on chart).

The months of August or early September were occupied in negotiations for working out financing that was necessary, and, in brief, the proposal was this, that the Land Trust Certificate arrangement would produce net \$1,250,000 towards the purchase. That was to be obtained—may I walk over here and point it out, your Honor?

The Court: Yes.

Mr. Stoel: A trustee for the Land Trust Certificate holders, The Union Trust Company of Cleveland, was to be the principal Trustee, let us say, and Security Savings and Trust Company of Portland was to be Co-Trustee in order to hold title to the property in Oregon.

The proposal was that the Security Savings and Trust and The Union Trust would sell \$1,350,000 face value of Land Trust Certificates and that, realized from that, they are to deposit into this purchase fund \$1,250,000. In return for that, the Union Trust Company and the Security Savings, as Trus-

tee for [4] these Land Trust Certificate holders, would receive the fee in the property, and that fee would be held, under the theory of the Land Trust Certificates, for the benefit of the Land Trust Certificate holders, each of whom would be entitled to an undivided equitable beneficial interest in the real property in the amount of his respective holding. If one held one share or one Land Trust certificate, he would have 1/1350th equitable interest in the real property. So it was to be \$1,250,000 from that source.

The arrangement further was that Building Syndicate, a local corporation, was to raise and to purchase a 99-year leasehold in the property with approximately \$950,000 to go in to make this total, and its funds were to be made up of corporate funds or else the sum of \$300,000 worth of stock that was subscribed for, and they had made arrangements and were in the course of making arrangements in August with Lumbermens Trust Company, a local trust company, to issue these first leasehold mortgage bonds in the amount of \$750,000, which Lumbermens Trust Company would underwrite in that amount, and then sell, and that was to produce additional funds to make up the \$950,000.

These arrangements, as I say, took considerable negotiations in working out the documents between early August and September, and they culminated in a final closing of this entire purchase in escrow to Title and Trust Company on September 30, 1927, and the parties to the escrow generally were Northwestern National [5] Bank, Building Syndicate, the

Lumbermens Trust Company, and they were Union Trust Company and Security Savings and Trust Company, Trustee and Co-Trustee, and the part that each of them was to play in the escrow and the documents and the money that they were to put in were as shown here generally.

In other words, Union Trust and Security Savings were to deposit \$1,250,000, and Building Syndicate was to put in whatever amount was additional to the leasehold bond money that came in that was on the \$950,000, and that would give us a total of two million two to go to the seller.

That amount being deposited, the seller was required to give a deed to Security Savings and Trust Company as Trustee.

In the same escrow there was deposited a leasehold mortgage indenture from Building Syndicate to Lumbermens Trust under which this company mortgaged its leasehold to Lumbermens Trust.

Also, in the deposit in escrow was a form of lease from Security Savings and Trust to Building Syndicate, a 99-year lease with option to renew and with option to purchase, requiring payment of annual rentals and so forth.

With those documents deposited and the money deposited the escrow was consummated, and the documents came out to the parties, as shown by the arrows here, and, as already explained, the money was deposited and went to the owners of the Northwestern National Bank.

The Court: What was the price mentioned in the

option from [6] Union and Security Savings to Building Syndicate?

Mr. Stoel: This option price is \$1,417,500 from Union Trust to Building Syndicate. I think this is a general outline of the transaction.

As I say, when the escrow was closed, it is our view of the transaction that the interests of the parties were as illustrated here; that the property was owned by the Trustee for the Land Trust Certificate holders who held—it is our theory as we see this case that the Land Trust Certificate holders held beneficial interest in the real property itself in the sums represented by their fractional holdings of certificates. Building Syndicate has purchased here, as we see it and we believe and sincerely allege, a leasehold for 99 years plus this option to purchase for \$950,000. The people who bought bonds from Lumbermens Trust Company simply held a first mortgage bond on the leasehold. That was their security, and they were to receive their interest on those bonds.

The Court: When you say purchased a leasehold, do you mean the \$950,000 was in addition to an annual rental that was going to be paid?

Mr. Stoel: That is right, your Honor. Now, just to complete the picture on this and to show how we get down to the plaintiff in this case, let me say first that there is sometimes a little confusion in names here.

The Court: How does the lessee purchase the leasehold? [7]

Mr. Stoel: How does the lessee purchase a leasehold?

The Court: Yes.

Mr. Stoel: I think he purchases it by obtaining a document which is a lease, which grants him a lease for the particular period and making payment of some money either directly or over a period of years for which he purchases it by that means.

The Court: He purchased that from the Security Savings?

Mr. Stoel: That is right. That is our concept of the transaction because at the moment that Building Syndicate purchased the leasehold Security Savings had just secured the fee in the simultaneous escrow proposal. In other words——

The Court: That was not money that was moving to Security Savings and Trust, though, was it?

Mr. Stoel: No; it was money which made it possible for Security Savings and Trust to receive a deed to the fee.

The Court: But what beneficial interest did Security Savings and Trust get out of it?

Mr. Stoel: It is our view that Security, as representative of the Land Trust Certificate holders, received an ownership in the property subject to this outstanding leasehold. That is what we would say.

Now the name of this company formed in 1927 was Building Syndicate. It ran into difficulties in the 30's with the depression, and finally in 1943 the leasehold bondholders foreclosed, and in a reorganization proceeding the present [8] plaintiff, Build-

ing Syndicate Co., was formed, and the interests of Building Syndicate, the assets including its leasehold and other assets, were transferred in that reorganization proceeding to the present Building Syndicate Co.

That was, as the parties have stipulated here, a tax reorganization so that the tax basis of the predecessor Building Syndicate was acquired or passed over to the new corporation, Building Syndicate Co., the plaintiff here.

The Court: The stockholders also transferred their interests?

Mr. Stoel: Actually, the stockholders, the old stockholders were wiped out in fact in that reorganization. As things actually worked, really actually happened when you look at it, what happened is that the bondholders came out the new owners.

The Court: And the bondholders then transferred their interest to the new corporation?

Mr. Stoel: In this reorganization proceedings they received income, bond, and stock in the corporation. That was accomplished in 1944 actually.

In 1945 the plaintiff, owning the leasehold which it had acquired through this reorganization, exercised its option to purchase the Trustee and paid the option price, acquired at that moment the full ownership of the property, and, we contend, is entitled to add that price then paid to its base for [9] the property, and after reallocating that gross price between land and building, acquired a new depreciation base on the building from that date forward in 1945.

The issue in this case, if we can state the issue in rather complicated notes as simply as possible, I think, as we see it, is whether or not in 1927, when the Northwestern Bank Building was sold, the documents which were transferred created the interests which appeared, we believe, from the face of them they were intended to transfer, or whether it can be said that the intent of the parties, despite the formal wording of the documents, was simply to create a mortgage in the Land Trust Certificate holders and their Trustee with the ownership of the building and property being in Building Syndicate.

We believe that the documents correctly state just what the transaction was. We believe our evidence this morning will show that that was what the parties intended; that is, that they intended to create exactly those interests, and that we believe further that in those circumstances the cases do not permit a holding that the transaction was a mortgage rather than, as the documents indicate, a deed with a leasehold value.

The Court: What is your explanation, Mr. Stoel, of the early returns of the syndicate, tax returns?

Mr. Stoel: I think the early returns—I might say first it is our view that these early tax, these early returns really do not constitute evidence of the intent of the parties that we [10] are looking for in this transaction.

I think the cases will show that in order to find a deed absolutely on its face subject to a mortgage, that the intent of the parties that it must be subject to that mortgage must be shown, and I think they

will further show that that intent must be present in the minds of both parties.

I think they will also show that the unmanifested, let us say, secret intent on the part of one of the parties that it would be considered a mortgage does not constitute the kind of use really to attach any mutual intent to that effect. If that intent was communicated to the other party and if he acquiesced in it, then I think you have a situation where that type of evidence will be proper to show mutual intent that the deed absolutely should be a mortgage, but in the absence of some communication of that evidence to the grantee in this case, the Union Trust Company, and in the absence of some communication that the grantee acquiesced in that manifestation and said, "That's our view," or by silence acquiesced in it, I don't believe that the evidence on how we treated this on the tax returns or other evidence subsequent to this acquisition really gets to the point of what the intent of the parties was. In other words, the intent of one side cannot create a mortgage unless it was communicated to and acquiesced in by the other.

That answers the question very obliquely. Let me say that so far as the tax returns are concerned we do claim depreciation [11] so-called on this, and on the tax returns for these years we entered deduction for depreciation on our tax returns under that heading. I think that was in error. It was, I think, a fairly natural error in view of the, it is fair to state, confusion with respect to the tax obligations or applicability of the tax, let's put it that way, to this

type of transaction in 1927, but I again want to say it is our view that that really does not go to the question that I think will be before the Court here as to whether the parties intended a mortgage.

I think it will take something more than just the unilateral evidence of how we, as we believed at that time, erroneously displayed some facts on our tax returns to show that Union Trust Company, the other party to this transaction, acquiesced in that.

It might be helpful, perhaps, in keeping this thing straight—I don't want to make an extended argument, your Honor.

The Court: I realize that.

Mr. Stoel: I could, if you like, just run through the points that we think our evidence will show and be particularly pertinent to this issue of intent of the parties. It may help your Honor in assessing the evidence as it comes in.

Generally, those points will be the one I just made; namely, that the parties must both intend that the deed is a mortgage for the intent of one is not enough; that there must be mutual assent to that fact.

We will show, I think, by evidence of both an officer of [12] the plaintiff and an officer of the Union Trust Company that no mortgage was intended. We will show that there must be a deed—excuse me—must be a debt before a deed can be construed to be a mortgage, and we will show that there is no debt where, as here, the payment of the supposed debt is optional with the supposed debtor.

There is one further point here that I think will

be of interest to your Honor to keep in mind as this evidence comes in, and that is that this is not a common case where the owner of land, subject to existing debt, refinances that debt by making conveyance to a third party and taking an option back from that party to purchase the property. In other words, we do not have here a situation where A with a mortgage on his property of a million dollars, let us say, conveys it to the Union Trust Company and gets a million two or a million three for it and has option to purchase it back at a million five and then pays off the mortgage and so forth. This is a situation where the Building Syndicate, holding no previous interest in this property, procured the conveyance of the property to the Union Trust Company and got back a lease and an option. In other words, this is a three-party transaction, but the property was never in Building Syndicate. It was in the Northwestern National Bank.

The conveyance by the Northwestern National Bank to the Trustee was procured by Building Syndicate, and we received back, Building Syndicate received back, a lease and an option. It [13] is our view that the rule in that situation is that the transaction is not a mortgage, and it is a situation to be sharply distinguished from that in which the refinancing operation and the conveyance by an owner of a previously existing interest in the property, in which he conveys it in return for an option or less value.

I will be glad to answer any other questions. This is rather a complicated original transaction. If there

is anything I can clarify going forward, I will be glad to do it.

The Court: You may proceed.

Mr. Stoel: Your Honor, we have marked here a substantial number of exhibits which are identified in the pretrial order. I was going to suggest that these might be put in now, but if Mr. Biggins has something perhaps that would be something more appropriate.

The Court: Mr. Biggins?

Mr. Biggins: I have had opportunity to examine documents in the pretrial exhibits 1 through 20 and have no objection to their being offered in evidence without further contest.

Mr. Stoel: Your Honor, we have identified, as Mr. Biggins told you, Exhibits 1 through 20. We are going to offer at this time—I can list them by number if you wish to describe them, or there are four or five that we are not going to offer immediately.

The Court: As soon as you are through with your opening [14] statement, then we will have Mr. Biggins' statement, and then you can make your offers, describing each exhibit and making some brief description so that I will understand what it is.

Mr. Stoel: Thank you.

Mr. Biggins: Very briefly, your Honor, Old Company, if I may refer to Building Syndicate as Old Company and Building Syndicate Co. as New Company—over the years the value of the American National Bank Building of course increased

substantially from the depression years into the post-war years. Knowing that, New Company went through a tax reorganization and acquired tax benefit of that tax reorganization. In consequence of that, they must assume the tax burdens of predecessor Old Company, which brings us to this.

Your Honor inquired the option price figure which is \$1,417,000. You may want to know how that is broken down for future reference during the trial. The option price of \$1,417,000 if we can round it off, as Mr. Stoel said, they only got \$1,250,000 so \$100,000, your Honor, is discounted so they sold it to the public, but there is also provision in the certificate that that can be redeemed at any time on option of the lessee, and the premium on redeemed is \$50.00 a share. The premiums on 1350 certificates will come to \$67,500. Those two components will be the difference between what was received in the escrow arrangement and the option price.

The transactions, as I understand them, first are addressed [15] to the Court on the intent of the parties. At this time I am a bit at sea. I don't know if plaintiff is conceding that the intent on the one side was as good as it was that this should be a mortgage transaction. If they are conceding that, I will accept that as a stipulation and restrain my cross-examination to that area; otherwise, it might have been an "even if" proposition, and I certainly don't want to restrict what we are going to do, Mr. Stoel, this morning. We are not conceding that.

Moving on to the Union Trust Company to the present plaintiffs, of course, we cannot anticipate

whether—we will have to see what the direct examination and the cross-examination will show.

On the arrangement here, there is no definite promise to pay a definite sum of money. We say that the certificate consideration here, just as it was in Lazarus and in Neighbors, there is no definite promise to pay and they had the same certificate issue which the Courts say was equivalent to a mortgage, being analogical to a loan arrangement, which we say this whole transaction was.

Now that the Court has considered the pretrial memorandum and the pretrial briefs of the parties, I believe there is nothing further to add unless you have questions.

The Court: What might be your position, Mr. Biggins—and I think this might be entirely outside the issues as raised—as to the equitable ownership value of the investment between [16] Builders Syndicate and the Land Trust Certificate owners?

Mr. Biggins: Do you mean——

The Court: What I am thinking is this: Suppose that immediately after the organization for some reason there was required a liquidation. It would appear to me that there would be an equitable interest then if we would look at it from that viewpoint, an equitable interest of Building Syndicate in the fund. Now this is just some thinking that I have been doing since looking at that chart. It is not just a hot and cold proposition here as to whether it should be definitely one way or the other. There possibly might be some medium ground there. I am just throwing that out for your consideration.

Mr. Biggins: My analysis would be this, your Honor: The market could go only two ways, up, down, or stay where it is. Staying where it is won't advance our thought. If the market goes up and the building is sold while the instruments are still in escrow, it is my belief and would be my contention that the proceeds from the sale would all go to Building Syndicate and that Building Syndicate would only be obliged to at premium, I concede, the Land Trust Certificates in the outstanding debentures.

Otherwise, if the market dropped and somebody is caught in a scissors, it will be Building Syndicate, and I further would concede that if the market dropped far enough that Security Savings and the indenture holders under the Oregon law would [17] have the right, which the legal instruments on their form says they do; namely, the holders of legal title and the bondholders of secured leasehold bonds then would be squeezed out.

The equity capital is in Building Syndicate. They are the owners. It is just as if this person loses 80 per cent on a loan. When the market drops 20 per cent, it is this man that is squeezed out; not here (indicating on chart). The key to the legal title is here, simply a security arrangement in the over-all view, which is our contention.

The Court: You may proceed now, Gentlemen.

Mr. Stoel: Your Honor, I would like to introduce at this time the following pretrial exhibits. I will describe them very briefly as I present them.

First is a letter of George W. York & Company

to Mr. George N. Black and Strong & MacNaughton Trust Company, dated June 21, 1927. This is referred to as a commitment letter, and I will accept that for it.

The Court: The first one was number what?

Mr. Stoel: Plaintiff's Exhibit No. 1.

The Court: That is admitted.

(Document above referred to and described, previously marked Plaintiff's Exhibit 1, was received in evidence.)

Mr. Biggins: If the Court please, if the Court thinks it would save time if they make a blanket offer of the exhibits listed 1 through 20, we have no objection. [18]

The Court: Do you want to handle those in that manner?

Mr. Stoel: No, there are some exhibits I am not ready to introduce at this time, your Honor.

The Court: Then you proceed. Thank you, Mr. Biggins.

Mr. Stoel: The second exhibit is Plaintiff's Exhibit 2 which is the original Minute Book of Building Syndicate. We have designated material set forth in the first 48 pages of that Minute Book as the Exhibit No. 2.

The Court: Admitted.

(Pages in Minute Book of Building Syndicate designated as Plaintiff's Exhibit No. 2 for identification were received in evidence.)

Mr. Stoel: Plaintiff's Exhibit 3 is a copy of a

prospectus published by the Union Trust Company, relating to Land Trust Certificates.

The Court: Admitted.

(Document above referred to, previously marked Plaintiff's Exhibit 3 for identification, was received in evidence.)

Mr. Stoel: Plaintiff's Exhibit 4, Deed from Northwestern National Bank of Portland to Security Savings Trust Company.

The Court: Admitted.

Mr. Stoel: A photostatic copy, your Honor.

The Court: Admitted.

(Photostatic copy of Deed above mentioned, previously marked Plaintiff's Ex. 4, was received in evidence.) [19]

Mr. Stoel: Plaintiff's Exhibit 5 is a photostatic copy of Assignment of Lease from Northwestern National Bank to Security Savings and Trust Company.

Mr. Biggins: We have no objection to photostatic copies.

Mr. Stoel: I was also going to say that we had referred to this Northwestern National Bank fee up here, and the deed which has just been offered is a deed to the fee. In addition, the Northwestern National Bank had a lease itself on a small parcel of property near the rear of their building. That is referred to as Parcel B, and A being the fee; Parcel B being, appearing by leasehold as a part of selling, involved selling that leasehold to Security Savings and Trust Company.

The Court: Admitted.

(Photostatic copy of Assignment of Lease above referred to, previously marked Plaintiff's Ex. 5 for Identification, was received in evidence.)

Mr. Stoel: Plaintiff's Exhibit 6, Agreement and Declaration of Trust between Security Savings and Trust and Union Trust Company as Co-Trustee and The Holders of Land Trust Certificates of Equitable Ownership.

The Court: Admitted.

(Booklet above described, previously marked Plaintiff's Exhibit 6 for identification, was received in evidence.)

Mr. Stoel: Plaintiff's Exhibit 7 is an Indenture of Lease from Security Savings and Trust, Lessor, to Building Syndicate, [20] Lessee.

The Court: Admitted.

(Booklet, Indenture of Lease, Security Savings and Trust, Lessor, and Building Syndicate, Lessee, previously marked Plaintiff's Exhibit No. 7 for identification, was received in evidence.)

Mr. Stoel: Plaintiff's Exhibit 8 is the Leasehold Bond Indenture between Building Syndicate and Lumbermens Trust Company.

The Court: Admitted.

(Document above described, previously marked Plaintiff's Exhibit No. 8 for identification, was received.)

Mr. Stoel: In the marking here we have a transposition.

The Court: Change it to the numbers in the pre-trial order.

Mr. Stoel: All right, the present number 10 becomes number 8.

Plaintiff's Exhibit 11 is a Deed from The First National Bank of Portland, Trustee, to Building Syndicate Co., dated October 27, 1945. That is correctly designated, your Honor.

The Court: Admitted.

(Document above described, previously marked Plaintiff's Exhibit 11 for identification, was received in evidence.)

Mr. Stoel: Plaintiff's Exhibit 12, Assignment of Lease from The First National Bank of Portland, Trustee, to Building Syndicate Co., dated October 29, 1945.

The Court: Admitted. [21]

(Document above described, previously marked Plaintiff's Exhibit 12 for identification, was received in evidence.)

Mr. Stoel: Plaintiff's Exhibit 13 is a Quitclaim Deed from Building Syndicate to Building Syndicate Co., dated February 14, 1945.

The Court: Admitted.

(Document above described, previously marked Plaintiff's Exhibit 13 for identification, was received in evidence.)

Mr. Stoel: Plaintiff's Exhibit 14 is a Quitclaim Deed from The National City Bank of Cleveland to Building Syndicate Co.

The Court: Admitted.

Mr. Stoel: Dated in 1945.

(Document above described, previously marked Plaintiff's Exhibit 14 for identification, was received in evidence.)

Mr. Stoel: Plaintiff's Exhibit 17 is a Booklet issued by George W. York & Co., entitled "The Land Trust Certificate Analyzed for Investors."

The Court: Admitted.

(Booklet above referred to, previously marked Plaintiff's Exhibit 17 for identification, was received in evidence.)

Mr. Stoel: Plaintiff's Exhibit 19 is a Memorandum of Option from The Northwestern National Bank to George N. Black.

The Court: Admitted.

(Document above described, previously marked Plaintiff's Exhibit 19 for identification, was received in evidence.) [22]

Mr. Stoel: Plaintiff's Exhibit 20 is a Memorandum of Extension of Option made as of August 6, 1927, from Northwestern National Bank to George N. Black.

The Court: Admitted.

(Document above described, previously marked Plaintiff's Exhibit 20 for identification, was received in evidence.)

Mr. Stoel: Those are the exhibits which we would like to have admitted at this time, your Honor.

We will call Mr. Harry C. Kendall. [23]

HARRY C. KENDALL

a witness produced in behalf of Plaintiff, having been first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Stoel:

Q. Can you hear me all right, Mr. Kendall?

A. Yes.

Q. What is your present position with the plaintiff, Building Syndicate Co., Mr. Kendall?

A. President.

Q. Are you a member of the Board of Directors?

A. Yes.

Q. How long have you held those positions?

A. Since the organization of the company.

Q. That was about when?

A. Pardon me? Well, I am practically sure since I was President of the old company and until the new company was formed and possibly for some time after that that I was elected President of the new company. I am not sure about the exact date.

Q. What was your occupation in 1927, Mr. Kendall?

A. I was President of the Lumbermens Trust Company.

Q. What were your duties generally there at that time?

A. Originating bond issues.

Q. What was your relationship or interest in the

(Testimony of Harry C. Kendall.)

Building Syndicate, the predecessor of Plaintiff here?

A. I was, I believe, approached by Mr. Black, and afterward I [24] learned about this deal, the proposed sale of the Northwestern Bank Building, and Black presented the proposition to me of the possibility of financing it through——

Mr. Biggins: If the Court please, we are going to object to the narrative type of question and answer. The question should be put in proper form so that the Government can object, have the opportunity to object as hearsay.

The Court: Yes; the answer is not responsive to the question. Would you please ask a new question?

The Witness: What was my interest?

Q. (By Mr. Stoel): I asked you first of all what was the relationship, your relationship with the Building Syndicate, a predecessor of the Plaintiff? Let me ask him direct questions on that point.

Were you one of the original stock subscribers of stock of Building Syndicate? A. Yes.

Q. Did you have any part in helping obtain other stock subscriptions from other people?

A. Yes.

Q. Did you hold an office when the corporation was first organized? A. Yes.

Q. What was that office?

A. Vice President. [25]

Q. Did you hold——were you——

A. Pardon me. I have to correct that. I don't

(Testimony of Harry C. Kendall.)

think that was immediately on the organization but very shortly after.

Q. Were you also a director? A. Yes.

Q. Did you continue as director and vice president throughout the life of that corporation?

A. Yes.

Q. That was until about what year?

A. 1927 to 1944.

Q. Was the property known as the Northwest Bank property for sale in the spring of 1927?

A. Yes.

Q. Who was handling the Northwestern Bank affairs at that time, generally?

A. O. L. Price, Trustee of the Pittock Estate, the U. S. National and the First National Banks.

Q. What was the reason for those parties having general control of the affairs of the Northwestern Bank?

A. The Northwestern Bank had gotten into financial difficulties, and the other two banks had taken it over so to speak, and Price was representing it, I presume as principal stockholder in the Northwestern National.

Q. What was the reason for the sale, if you know? Was there a liquidation in process with respect to the Northwestern Bank [26] properties?

A. Yes.

Q. Who was George N. Black in 1927? Did you know him?

A. He was a real estate broker in Portland.

(Testimony of Harry C. Kendall.)

Q. Did he have an interest in attempting to sell the Northwestern Bank property?

A. Yes; he hoped to make a commission.

Q. Did you discuss the sale of the property with him? A. Yes.

Q. What did you understand the price to be?

A. Two million two hundred thousand, I think.

Q. Did you have any understanding from him as to what the sellers required? A. Yes.

Mr. Biggins: I object to the form of the question; conclusion of the witness.

The Court: It is a conclusion of the witness.

Q. (By Mr. Stoel): You say the price was \$2,200,000. Was it payable all in cash?

A. Yes.

Q. What was your interest in seeking information with respect to the proposed sale of this property?

A. To obtain a bond issue for the Lumbermens Trust Company, and when I saw the possibility of acquiring the use or income use of a valuable property for a small investment, I became [27] interested in obtaining the stock interest in the lessee corporation.

Q. Did you discuss with Mr. Black how the property might be acquired? A. Yes.

Q. What was that discussion?

Mr. Biggins: Objection; hearsay, your Honor.

The Court: On what theory do you believe that is admissible, Mr. Stoel?

Mr. Stoel: I think the witness, your Honor,

(Testimony of Harry C. Kendall.)

ought to be able to tell us what the background of the acquisition of this property was and the information which he had which led him to acquire an interest in it.

The Court: He can testify as to what information he may have had, but I do not believe hearsay is proper under those circumstances. The objection will be sustained. You are entitled to put in evidence to place the Court in the same position the parties were in at the time.

Q. (By Mr. Stoel): Do you know whether Mr. Black had an option for the purchase of this property? A. Yes; he did.

Mr. Biggins: We will stipulate that he did. Exhibits 19 and 20 are true copies of that option.

Q. (By Mr. Stoel): Did you have any discussion with Mr. Black before the date of this option which I think the record will show [28] is July 7, 1927? A. Yes.

Q. Did you work out in your own mind any plan for the financing of that property?

Mr. Biggins: I object to that; speculative and a conclusion.

The Court: The objection is sustained.

Q. (By Mr. Stoel): Mr. Kendall, you have stated that you were one of the original subscribers to the stock of this Building Syndicate and also that you obtained subscriptions from other people with respect to stock of this corporation?

A. Yes.

Q. In obtaining those subscriptions, what did

(Testimony of Harry C. Kendall.)

you describe as the transaction in which this corporation proposed to engage?

Mr. Biggins: I object to that. That calls for a declaration. The Government is not bound by it. The objection is hearsay, your Honor.

The Court: It does call certainly for a conclusion of the witness. The objection is sustained.

Mr. Stoel: Your Honor, I think that in this connection the point of this testimony is to show what kind of transaction the subscribers, including Mr. Kendall, thought they were entering into here. I think that will become pertinent on the question of what they intended this transaction to be.

Mr. Biggins: I have no doubt, your Honor, that would be pertinent if competent. The objection is on the basis of competency [29] here. There is objective evidence that exists here, the minutes of the Board of Directors meeting, but we certainly are not going to be bound by hearsay and self-serving testimony of the single surviving witness apart from these minutes, what was said to persons now deceased. If he can establish—I agree if he can establish conversations with living persons whom we can bring in the courtroom for cross-examination, he can go ahead and testify.

The Court: I do not think that would be the rule, Mr. Biggins. I do not think that is it, but I do think there is merit in the thought that whatever went forward there was finally reduced to the minutes of the corporation. Is there a claim of ambiguity in the minutes of the corporation? If

(Testimony of Harry C. Kendall.)

there is, then I will permit the evidence; otherwise, I would say we are bound by the minutes.

Mr. Stoel: Your Honor, I think there will be a claim of ambiguity. There certainly will be a definite question of interpretation of those minutes between Government counsel and ourselves. I think this will be pertinent from that standpoint.

The Court: I will permit the testimony solely on that ground.

Q. I have asked you, Mr. Kendall, how did you describe the transaction to the people whom you were soliciting for subscriptions to the stock of this corporation, the proposed transaction this corporation would enter into? [30]

The Witness: I told them that it was proposed this property would be sold to the Union Trust Company and George W. York as Trustees or a Trustee representing them as Trustee for the Land Trust Certificate owners and that the Trustee would give to Building Syndicate Co., a lease in exchange for money, a promise to pay rentals, and also there would also be an option.

This deal was pretty well set up by Black and George W. York and Company before I came into it so that my interest was in acquiring a leasehold bond issue for the Lumbermens Trust Company.

Mr. Biggins: We are getting into unresponsive testimony, your Honor. I object.

The Court: That is correct. The last portion may be stricken. You may ask another question, Mr. Stoel.

(Testimony of Harry C. Kendall.)

Q. (By Mr. Stoel): You have said, Mr. Kendall, that you yourself purchased stock in this corporation? A. Yes.

Q. Why did this transaction seem attractive to you as an investor?

A. Well, Strong & MacNaughton Trust Company assured me that the rental income could be materially increased, and if it could I thought the proposed lease terms would be attractive and possibly that we would ultimately be able to exercise the option to acquire the property if the earnings panned out as well as indicated. [31]

Q. I think the record will show in Exhibit 2, the minute book, that this corporation was organized on August 5, 1927, and the stock subscriptions, I think, are assigned on the same date.

After the organization, then, Mr. Kendall, did Building Syndicate secure from Mr. Black his option in any way? A. Yes.

Q. That option, I believe it will show—that's Exhibit No. 19—was about to expire, I think, on August 7th. Was an extension of that option secured? A. Yes.

Q. You were then an officer and Director of Building Syndicate, then, at this time we are talking about from August 7th onward?

A. I think so. I am not too clear as to the exact dates right in there.

Q. What steps were taken by Building Syndicate, then, to consummate the arrangements look-

(Testimony of Harry C. Kendall.)

ing toward the ultimate sale to the Land Trustee of the Northwestern Bank property?

A. An escrow was arranged with the Title and Trust Company so that all the—to represent all the parties involved.

Q. Was that preceded by any negotiations with respect to the terms of an instrument that would be part of that escrow? A. Yes.

Q. With whom were those negotiations conducted? Who were the parties that would be involved in those negotiations?

A. The Union Trust Company of Cleveland in regard to the fee [32] and the Land Trust Certificates; the Lumbermens Trust Company as to the underwriting of the bond issue, and the Building Syndicate Co. as to the funds derived from the sale of leasehold bonds plus the funds derived from the sale of stock, and, of course, the Northwestern National Bank as to the delivery of title of the property.

Q. Was Mr. Black one of the original subscribers to the stock of Building Syndicate?

A. Of this first group, yes.

Q. Did he remain interested in the corporation for any substantial period?

A. No; a very short time. In fact, I don't know whether any stock—I don't think any stock was actually delivered to him.

Q. In the completion of the escrow, Mr. Kendall, what documents did the various parties receive?

(Testimony of Harry C. Kendall.)

A. Securities Savings & Trust Company as Co-trustee of the Land Trust Certificate owners received a deed to the property.

Building Syndicate received a 99-year lease with option to purchase.

Lumbermens Trust Company received an indenture of lease.

Q. I beg your pardon. I couldn't hear that last, Mr. Kendall.

A. Received an indenture of lease for the leasehold bonds.

The stock subscribers received stock.

Q. Did Building Syndicate ever exercise the option that [33] Mr. Black had assigned to it from Northwestern National Bank? A. No.

Q. How did it acquire the property if it didn't exercise the option? How was the property closed out here?

A. It was arranged through this escrow.

Mr. Biggins: I object, your Honor. That method will be set forth in the legal instruments.

The Court: The best evidence would be the written instruments if they are available. I understand they are.

Mr. Stoel: I withdraw the question, your Honor.

Q. As an officer and Director of Building Syndicate at this time, Mr. Kendall, what interest did you believe Building Syndicate had in the property when the transaction was consummated?

Mr. Biggins: I object to that; calls for a conclusion.

(Testimony of Harry C. Kendall.)

Mr. Stoel: Your Honor, I think the question is going to be intent of the parties. This man was the Vice-President and Director at the time. I think his understanding of the transaction and what the company got out of it—except for the issue being raised by the Government here.

The Court: It would not be his only understanding. If the question was if he knows what matter was the understanding of the Directorate of the group there, I will permit an answer to that question. However, it still must be on the basis that there is an ambiguity in some of the documents because the Court will have to construe the documents and get from that the [34] intention of the parties, and if this will go to put me in better position to understand the evidence then I will hear it, but only for that purpose.

Q. (By Mr. Stoel): Will you answer the question, Mr. Kendall?

A. Neither I nor anybody else involved had the remotest idea that we were getting anything but a lease.

Q. Did that lease contain a purchase option as well? A. Yes.

Q. Did you believe and, if you know, did the other Directors believe that Building Syndicate owed any debt to the Trustee of Land Trust Certificate holders? A. No; definitely not.

Q. What did you believe and, if you know, what did the other Directors believe?

(Testimony of Harry C. Kendall.)

A. Pardon me, except, of course, for the payment of rental.

Q. Yes. What did you believe and, if you know, what did the other Directors believe would happen if Building Syndicate defaulted in its lease obligations? A. They would cancel the lease.

Mr. Biggins: May it be understood, your Honor, I have a running objection?

The Court: I understand it, and the evidence is being received solely on the theory if there is an ambiguity it may be used by the Court for that purpose.

Mr. Biggins: My objection also extends to the competency [35] of this witness to state what the positions of the other parties were.

The Court: I realize that.

Q. (By Mr. Stoel): Can you answer my question, Mr. Kendall, or do you want it repeated?

A. I understood that if we didn't pay the rental on time that the lease was subject to cancellation on 60 days' notice.

Q. Did you believe that Building Syndicate could claim a right to redeem the property from the Trustee for the Land Trust Certificate holders in the event of cancellation of the lease?

A. No; never had any such idea, and nobody else did.

Q. Did you participate in these negotiations during August and early September in respect to a form of lease and the proposed agreement with Union Trust Company? A. Yes.

(Testimony of Harry C. Kendall.)

Q. Did you as an officer and Director in participating in those negotiations ever represent to Union Trust Company at that time that you thought that Building Syndicate would have a right to redeem the property in the event of a cancellation of the lease? A. No.

Q. Was a representative of Union Trust Company in Portland in connection with the negotiations we are describing? A. Yes.

Q. Who was he? [36] A. A. C. Coney.

Q. To your knowledge, did he or any other representative of the Union Trust Company represent in any way that the transaction resulted in a debt owing from Building Syndicate to Union Trust Company? A. No.

Q. Did he or any other representative, to your knowledge, represent that on default to Building Syndicate Co. by Building Syndicate in the lease terms that Union Trust Company could invoke only the rights of the mortgagee? A. No.

Q. Who is custodian of the corporate records of Building Syndicate, Mr. Kendall?

A. Mr. Brewster, Secretary.

Q. Who kept custody of these corporate records during the entire period of the existence of Building Syndicate and of the present claimant?

A. The Manager, one management firm.

Q. Can you tell me who those management firms were?

A. The first one was Strong & MacNaughton Trust Company, then Robert H. Strong & Associ-

(Testimony of Harry C. Kendall.)

ates, then Strong & Brewster. The firm is now known as Strong & Brewster—it is now Brewster, Scholz & Burnett.

Q. In the day-to-day operation of Building Syndicate and under present plaintiff, what was the practice? Did you as the [37] Vice-President and Director take active day-to-day management, or do you now? A. No.

Q. How is that handled?

A. By the Manager, the management firm.

Q. What is the function of the Directors, and what is their relationship generally to that operation?

A. Well, we have had two meetings this year. We pass on matters of major policy. Usually at the request of the management when they have some problem that they think should be passed on by the Directors, we have a Directors meeting.

Q. Other than a representative of the management firm who might be an officer of the company, would the other officers other than you do about the same as you have described as doing and not participate in the day-to-day activities?

A. Yes.

Q. Do you have any records of Building Syndicate, the original corporation here, in your possession?

A. No; except, say, occasional documents or duplicates or reports to stockholders, bondholders; in other words, no official corporate records.

Q. Have you searched your record that you do

(Testimony of Harry C. Kendall.)

have for an escrow agreement relating to the acquisition of Northwestern Bank property in 1927?

A. Yes; I did make a search, although I knew I didn't have it. [38]

Q. In the Minute Book, which is Exhibit 2, on Page 19, there is a reference to a proposed commitment from Union Trust Company. Have you searched your records for that proposed commitment? A. Yes.

Q. Did you find it? A. Didn't find it.

The Court: We will have a ten-minute recess.

(Recess taken.)

Mr. Biggins: May it please the Court, could we have handed to the witness, please, Exhibit 2, which is the Minute Book?

Mr. Stoel: Excuse me. There is one further matter I would like to put upon the record.

Mr. Biggins: Certainly; no objection at all. I thought you had finished.

Mr. Stoel: No; I am sorry. Will you hand this to the witness, please, Mr. Bailiff?

(Document presented to the witness.)

Q. (By Mr. Stoel): Mr. Kendall, there has been handed to you Plaintiff's Pretrial Exhibit 17, described as a booklet issued by George W. York & Co., entitled "The Land Trust Certificate Analyzed for Investors." Did you have this booklet in your possession during the negotiations for the

(Testimony of Harry C. Kendall.)

Northwestern Bank property that you have been describing? [39] A. Yes.

Q. Do you know where it came from?

A. George Black gave it to me.

Q. Did you form some of your ideas, at least as to the interests which the parties were to receive in this transaction, from that booklet?

A. Yes.

Mr. Stoel: That is all, your Honor.

The Court: You may proceed, Mr. Biggins.

Cross-Examination

By Mr. Biggins:

Q. Mr. Bailiff, would you pass the Minute Book, Exhibit 2, to the witness, please?

(Exhibit was thereupon presented to the witness.)

Q. To put one very small point at rest at the outset, Mr. Kendall, I believe you said that, as far as you knew, George Black subscribed for 1,025 shares of common stock in Building Syndicate, but he never paid for them. Was that a correct understanding of your testimony? A. No.

Q. What did you say?

A. I didn't say how many shares, and I didn't say he didn't pay for it.

Q. What was—— [40]

A. I said he subscribed to stock, and I don't think stock was ever issued to him because his stock

(Testimony of Harry C. Kendall.)

subscription was balanced off on this commission. In other words, he had fifty thousand commission coming, and he paid ten thousand for the option, and that was credited, so that I believe it left nineteen thousand perhaps which I think he arranged to sell to other parties, so I don't think any was ever issued for Black.

Q. It is true, is it not, Mr. Kendall, that he did pay \$10,000 for the option? A. Yes.

Q. And it is further true that it was agreed by the Board of Directors, of which you were a member, that that \$10,000 on assignment of option to Building Certificate would be credited to his stock subscription account? A. Yes.

Q. As was done on the books of the corporation?

A. I believe so.

Q. Subsequent to that, Mr. Kendall, looking at Page 19 one minute, which is Exhibit 2 before you, you see at the bottom of the page, sir, the language:

“It appearing to the Board that it will be necessary that the subscriptions to capital stock of this company be paid in cash”——

——incidentally, Mr. Reporter, if we go too fast we have these exhibits you could have later——[41]

——“in full on or before September 1, 1927.”

What does it say then, Mr. Kendall?

A. ——“in order to provide funds with which to effect the purchase of the Northwestern Bank Building property.”

(Testimony of Harry C. Kendall.)

Q. All right—

—“on motion duly made and seconded it was unanimously

“Resolved that this Board of Directors make a call upon the subscribers to its capital stock for payment in full to this corporation of the amounts of their respective subscriptions in cash on or before noon of August 29, 1927.”

Now, is there any entry after this, then, that you know of, Mr. Kendall, showing that Mr. Black did not pay his subscription as requested to do so?

A. Well, he didn't pay it.

Q. Thank you, sir.

Going to other matters now—by the way, who was the Secretary of that meeting, on Page 20?

A. That is Alfred A. Hampson.

Q. Do you recognize the signature?

A. Yes.

Q. What was his relation to the corporation other than Secretary?

A. He was the attorney. [42]

Q. He was an attorney. You have had a chance to refresh your recollection from these minutes, have you not, Mr. Kendall? A. I have.

Q. You are familiar with the minutes, are you not? You are familiar?

A. I have looked them over. I can't say that I am very familiar with them.

Q. Knowing you had to come to testify today, you refreshed your recollection from other corpo-

(Testimony of Harry C. Kendall.)

rate records and documents you had available to you? A. Yes.

Q. Can you point out to us, sir, one single document or one single page in the minutes of this corporation where it is stated that this property was being sold to the Security Savings & Trust Company? A. I don't believe, I don't—

Q. One such reference or one such document, Mr. Kendall; do you know of one?

A. Well, if there were two or three, I probably couldn't say that I remember them.

Q. You don't know of any at this time, do you?

A. I don't know whether I know of them or not. I can't even recall the name suddenly of a good friend of mine when I wanted to introduce him. If I may have a half a dozen documents, I couldn't sit here and tell them to you. [43]

Q. Reading the minutes of the corporation to refresh your memory, you did see many references to Building Syndicate purchasing this property; you did see those references, didn't you?

A. That's the way the wording would indicate.

Q. In these minutes; in these minutes.

A. But this wording is, I suppose, set forth in this way and, incidentally, I may never have read these minutes at the time. You know how the minutes of most corporations are handled. Somebody moves that the reading of the minutes be waived; somebody seconds it, and they are waived, and so you don't even read the minutes. It is generally just a perfunctory operation, so I didn't know what

(Testimony of Harry C. Kendall.)

the minutes said then probably, and I don't know now, except that I have looked over this book.

Now, this matter of referring to the exercise of the option or whatever it was by the building, the building never did—I mean the Building Syndicate Co. never—or Building Syndicate never did exercise the option. The option was exercised by the escrow agent with the co-operation of all the parties involved, and when we talk about buying a building we mean a group, the Trustee for the Land Trust Certificates actually was the one that bought the building or bought the property, and we got a lease. We were all parties to this involved transaction so that the wording in this book I don't think has any significance. [44]

Mr. Biggins: If the Court please, I request that the answer of the witness be stricken as unresponsive to the question.

The Court: Well, it certainly is not binding on the Court, Mr. Biggins. Therefore I will permit it to stand.

Q. (By Mr. Biggins): Do I understand it to be the practice with this Board of Directors in this corporation, Mr. Kendall, that the Minutes of the Board were considered of no importance and were not read at the subsequent meetings?

A. I would not say they were of no importance, but frequently the reading of the minutes is waived.

Q. Were they waived in this case?

A. I don't know.

Q. Addressing your attention, sir, to Pages 31,

(Testimony of Harry C. Kendall.)

32, 33, 34 and 35 of the minutes, sir, and these are in the Government's brief if the Court cares to see them, as an appendix—you see Page 31, sir? I am not asking you to read it, but glancing at it rapidly do you see Page 31? A. Yes.

Q. And 32 and 33, and in this meeting of the Board, as I understand, the various legal instruments were discussed?

A. All I know about this is what I read in this book. I naturally have no recollection of exactly what took place or when the meeting was held. All I can go by is what is shown in this book. [45]

Q. You have no recollection, then, of this meeting?

A. Well, after I look this over I might cudgel my brain to remember a little about it. **Do you** want me to take time to do that? I can't just look at the page from here and say I remember it.

Q. Would you look at Pages 32 and 33 rather closely for me, Mr. Kendall, please?

(Witness examines document.)

A. As far as my recollection is concerned, all I could say is——

Q. Before answering, Mr. Kendall, have you had time to examine Pages 32 and 33?

A. No; I haven't read them carefully. I hate to take all this time.

Q. That is all right.

(Witness again examines pages referred to.)

A. All I could say is I would not be able to ap-

(Testimony of Harry C. Kendall.)

prove these minutes as they read if I had had any idea of the necessity for precise and long-winded explanation of this complicated deal. We might say "we" when we are talking about the corporation or the whole group involved in this deal.

Q. Have you had an opportunity to read Pages 32 and 33, Mr. Kendall? A. Yes.

Q. All right, 34, would you glance at the first two paragraphs [46] of Page 34, sir, please?

A. Yes.

Q. Glancing over to Page 31, just indicating to you, a special meeting was called on September 19th, it says:

"The following Directors were present, Watzek, Taylor, Kendall and Luders, constituting a quorum of the Board."

You do recall being at that Board of Directors meeting now, don't you?

A. No. I assume I was there because it says I was, but I don't remember.

Q. Do you recall being at any Board of Directors meetings in which the Board as a body considered and approved a form of declaration that was to be used? A. Yes.

Q. They discussed it; they reviewed it; they approved it?

The Court: What trust agreement are you talking about?

Q. (By Mr. Biggins): Turning to Page 32, if it will help for a point of reference, Mr. Kendall, they first resolve:

(Testimony of Harry C. Kendall.)

“Resolved, that said printed form of Declaration of Trust,”

which is referred to as Exhibit A there which I assume, sir, is the same as the——

A. Yes; we looked over this, approved it.

Q. Discussed it? [47] A. Yes.

Q. And approved it? A. Yes.

Q. Do you recall any Board of Directors meeting in which the form of lease identified in these minutes as Exhibit 5 was reviewed?

A. Yes.

Q. Discussed; discussed, sir? A. Yes.

Q. And approved? A. Yes.

Q. Furthermore, a meeting in which the Board discussed the form of mortgage, over there on Page 33, identified as Exhibit C eventually, Mr. Kendall. Do you have the language there,

“Resolved, that said”——

A. ——“form of mortgage,” to the Lumbermens Trust Company.

Q. Yes, sir. A. Yes.

Q. And form of bond to be issued?

A. Yes.

Q. And the Board of Directors, as you recall, reviewed them? A. Yes.

Q. Discussed them? A. Yes.

Q. And approved them? [48] A. Yes.

Q. At any point here, if the Board of Directors of Building Syndicate had not approved the trust

(Testimony of Harry C. Kendall.)

agreement, this deal would have fallen through; now, wouldn't it?

A. You mean on the Land Trust Certificates?

Q. If the Board of Directors of Building Syndicate had disapproved the form of trust agreement presented at this meeting, this deal would have fallen through?

A. I presume it would unless it could be resolved between the parties.

Q. And by "resolved between the parties," you mean, sir, Building Syndicate and the Trustee?

A. Trustee for the Land Trust Certificate owners.

Q. Yes, sir. Is that who you mean by the parties, Mr. Kendall? A. Well——

Q. Well, who do you mean by the parties?

A. Well, actually, the negotiations were between Building Syndicate and the Union Trust Company and Lumbermens Trust Company. They were the parties that had to agree on this joint deal.

Q. And the Board of Directors so regarded this, as a joint deal?

A. Joint in that each party had a certain function to perform.

Q. The Board of Directors did regard this as a joint deal?

A. Well, it depends on what you mean by joint deal. I used [49] that term rather loosely. Now we are getting so precise I will have to be a little precise. Just what do you mean by joint deal?

(Testimony of Harry C. Kendall.)

Q. What did you mean when you responded to my question, sir, on the parties to this joint deal?

A. Well, what I meant was this, was that there were three parties here that have to agree on what each one is going to do; one of them is getting the ownership to this property, give another one a lease, and they are going to issue bonds, the third party.

Q. It was a package deal, then? Can we use the word it was a package deal?

A. It was a simultaneous deal.

Q. The escrow was simultaneous, but the negotiations were in a package, were they not?

A. Well——

Q. Do you want to consider it?

A. I don't know what you mean by "package." We had to agree, each one of us, on what part he was going to take in this deal, but it was not—what I am alluding to is this: A joint agreement, when I was in the bond business we had joint agreements, and we would all be in the agreement together as equal partners. Now there is no joint agreement in that sense of the word at all. We simply had a deal here in which three parties had to agree on each one doing certain things. [50]

Q. (Approaching blackboard): Building Syndicate had an option with Northwestern, didn't it, to buy that property for \$2,200,000; is that right?

A. Yes.

Q. Security Savings didn't have an option, did it?

A. No.

Q. Union didn't have an option, did it?

(Testimony of Harry C. Kendall.)

A. No.

Q. And none of the Land Trust Certificate holders? A. No.

Q. Building Syndicate didn't have enough money to buy that property, did they?

A. No.

Q. They only had \$300,000? A. Yes.

Q. So you got together a group as a syndicate to raise more money?

A. Not as a syndicate, no.

Q. Well, to raise more money?

A. No, not as a syndicate. It was——

Q. Union said it could sell some trust certificates, approximately \$1,350,000. Now that was negotiated first between Black and Union Trust, wasn't it? A. Yes.

Q. And a commitment made? [51]

A. Commitment with somebody else.

Q. George York, excuse me.

A. From York and Black, yes.

Q. Subsequent to which Union took over the commitment? A. Yes.

Q. And renegotiated the commitment with Building Syndicate? A. Not necessarily.

Q. Look at Page 45 of the Minutes, Mr. Kendall, and refresh your recollection, 45 and 19, 45 and 18, sir. What page do you have open before you?

A. 45.

Q. Let's turn back—well, I do not have 19 there. May I approach the witness, your Honor?

The Court: Yes.

(Testimony of Harry C. Kendall.)

Q. (By Mr. Biggins): Reading 45, do you recognize the signature? A. Yes.

Q. Well, these are in evidence on Page 45, aren't they, Tom?

Mr. Stoel: Yes.

Q. Well, reading, and you follow me mentally: "A communication was received from the attorneys of The Union Trust Company of Cleveland for a signed copy of the original commitment between The Union Trust Co. and the Building Syndicate. It was the decision of the Directors that as this commitment had never been signed that the deal had been [52] consummated without it, and that in the final closing of the transaction several modifications had been made rendering the commitment of no value and that it would not be possible to comply with their request."

Now, turning to Page 18, sir, and holding your finger at Page 45 if you want to refer back to it—19—do you see the language:

"There was also submitted a form of proposed commitment covering the purchase of the Land Trust Certificates by Union Trust Company and George W. York. Attention was called to the fact that this commitment contains a provision relative to the payment of interest on the interim certificates which was not contained in the original commitment. On motion duly made and seconded it was unanimously"—

And then the resolution changing it?

Does that refresh your recollection now, Mr. Ken-

(Testimony of Harry C. Kendall.)

dall, that a subsequent commitment was negotiated between Building Syndicate and Union after the original commitment with George Black and George York & Co.?

A. Well, all I can say is that I assume that it was from these minutes, and I cannot say that I remember. I do remember something about this interest that was asked for, and we objected [53] to it.

Q. Have we established, Mr. Kendall, to your satisfaction and recollection that a subsequent commitment was negotiated between Building Syndicate and Union?

A. No; I am afraid not. This Land Trust Certificates deal was set up before I had anything to do with this deal, between York and Black, and I can't recall any modification that was made on that.

I do have a hazy recollection about some argument about the interest that would be charged during some interim period, and we objected to it.

Q. Could I have Exhibit 3 handed to the witness, please?

In your hand, Mr. Kendall, is Exhibit 3 which is the prospectus or proposal of Union Trust Company to sell these certificates to the public. You are familiar with the certificate, sir?

A. Yes.

Q. That certificate was worked out with Building Syndicate, though, wasn't it—that prospectus, I mean, and Building Syndicate did work out and approve Exhibit 3, did it not? A. Yes.

(Testimony of Harry C. Kendall.)

Q. In fact, the minutes on Page 19, if you will look at it, Mr. Kendall, authorize and apparently directed you, sir, Mr. Kendall, to endorse the approval of this corporation thereon and forward the same to the Union Trust Company. Do you see that on Page 19? [54] A. Yes.

Q. Which you did? A. Yes.

Q. So this was worked out with Union Trust Company for Building Syndicate? A. Yes.

Q. Security Savings didn't have anything to do with that, did they, this prospectus here?

A. No; I don't think so.

Q. Northwestern Bank didn't have anything to do with that either, did they? A. No.

Q. Northwestern Bank didn't have anything to do with the commitment deal, either one or both? They were not part of the negotiations and had nothing to do with it, did they?

A. I would say they did. They understood how they were going to receive this money through this escrow arrangement.

Q. From Building Syndicate?

A. No; not from Building Syndicate. The money never went to Building Syndicate. We never had the money.

Q. Northwestern Bank took no participation in negotiations or changes in the original financial commitment with Union Trust for George York; now, that's true, isn't it? A. Yes.

Q. All right. Security Savings took no part in

(Testimony of Harry C. Kendall.)

the negotiations [55] or endorsement of the prospectus; we have established that, haven't we?

A. Yes.

Q. Nor did they take any part in the negotiations of the financial commitment, either the one between George Black and York Company or Union Trust and Building Syndicate, and they took no part in those negotiations, did they?

A. I would say they did.

Q. When, where, and who was there, Mr. Kendall, as you recall?

A. We were dealing all through this transaction with the Union Trust Company, with the Northwestern Bank, the Lumbermens Trust Company. The Security Savings & Trust Company, of course, were more or less passive in the whole matter. They were simply the Co-trustee acting for the Union Trust Company.

Q. It reduced down to this, didn't it, Mr. Kendall: Building Syndicate dealt with Union—right?

A. Yes.

Q. Building Syndicate dealt with Security Savings & Trust, negotiated with them? A. No.

Q. They didn't negotiate with them?

A. No; they negotiated with Union Trust, and Union Trust told Security Savings what to do, I would say.

Q. Are you saying Building Syndicate had no negotiations with Security? [56]

A. No, not what I would call negotiations.

Q. Building Syndicate had negotiations with

(Testimony of Harry C. Kendall.)

Lumbermens Trust, didn't they? A. Yes.

Q. Northwestern Bank? A. Yes.

Q. And their mortgage company, the company that had the mortgage on the building they owned?

A. It was understood when this money was paid that Northwestern Mutual would get their money out of it. We never had any negotiations with them directly.

Q. Well, let's look at the record.

A. That was arranged between Northwestern Bank and the Northwestern Mutual Life.

Q. Let's look on Page 27, Mr. Kendall, of the minutes, reading quickly the resolution that they have there on Page 27:

“Be It Resolved, that the President and attorney”—who is the attorney, again?

A. I presume it was Al Hampson.

Q. He was the one that was Secretary, as I recall, of these minutes we looked at; is that right?

A. I presume so.

Q. “Be It Resolved that the President and attorney of the company be and they hereby are authorized and directed to attend a meeting to be held at noon [57] of this day at the offices of Lumbermens Trust Company, at which meeting are to appear representatives of said Lumbermens Trust Company, First National Bank, United States National Bank and Northwestern National Bank, there to take such action as the President may deem necessary or advisable relative to extension from Northwestern National Bank of the

(Testimony of Harry C. Kendall.)

present option held by this company for the purchase of the Northwestern Bank Building property and/or relative to any other agreements required to be made with any of the organizations to be represented at said meeting for the purpose of making possible the completion of the proposed purchase of said Northwestern Bank Building property.”

Building Syndicate did have some negotiations with the people holding the mortgage on Northwestern, so far as you recall; now didn't they?

A. I don't recall that we did, but I can't see that it makes any difference; but I just don't recall.

Q. But Union Trust was not at that meeting we just looked at, were they? A. No.

Q. Or Security Savings weren't at that meeting, were they?

A. I presume not. They are not mentioned here.

Q. So, bringing it to a close, Mr. Kendall, the Board of Directors of Building Syndicate approved the financial commitment [58] with Union Trust; did they not? A. Yes.

Q. All right. And they approved a trust agreement that was subsequently drafted?

A. Yes.

Q. And they approved the mortgage?

A. Yes.

Q. And the bond issue? A. Yes.

Q. With Lumbermens Trust? A. Yes.

Q. And those were all approved on or around

(Testimony of Harry C. Kendall.)

the meeting of September 19, 1927, before these instruments were put in escrow?

A. Yes; I presume that they were. I would say that they were.

Q. And all of these instruments were delivered to Building Syndicate; all these executed instruments were delivered to the Building Syndicate?

A. I don't know whether they were or not.

Q. But you do know that Building Syndicate carried the ball from there to see that the escrow arrangement was carried out?

A. Well, Building Syndicate plus Black plus Strong & MacNaughton Trust Company were the pushers on the deal. The three were all involved and all co-operating to carry it through.

Q. As representatives of Building Syndicate?

A. As representatives of Building [59] Syndicate.

The Court: Who were representatives, Mr. Biggins?

Mr. Biggins: The people he just mentioned, sir. That will be on Pages 39 and 40.

Q. Would you take a quick look at Pages 39 and 40, Mr. Kendall? A. Yes.

Q. You see there on Page 39 that Strong & MacNaughton should appoint an agent. Now turning over to Page 40:

“After a general discussion of the situation existing relative to the proposed purchase of the Northwestern Bank Building property and statement that the escrow will probably be completed

(Testimony of Harry C. Kendall.)

by the delivery of the papers not later than the 30th instant, the Board directed the attorney to deliver to Strong & MacNaughton Trust Company, as the managers of the property, all original papers in his possession covering the purchase of the property.”

So Strong & MacNaughton were getting in this deal as the agents of Building Syndicate; weren't they? A. Yes.

Q. In closing that escrow?

A. Yes—well, no—I don't think in closing the escrow.

Q. Who closed the escrow, then, Mr. Kendall?

A. Well, I would say that all the parties involved closed it by unanimous approval and consent.

Q. Isn't this what happened now, Mr. Kendall? Exhibit A, [60] which is referred to as the draft agreement, was negotiated and approved by the Board of Directors, and the original submitted to the Board; that's true, isn't it? A. Yes.

Q. Exhibit B, which was the last I believe so negotiated and approved by the Board of Directors and the original executed and deposited with the Board of Directors? A. Yes.

Q. Exhibit C, a mortgage, was reviewed, discussed and approved, and the original executed and deposited with your Board of Directors?

A. Yes.

Q. Then an escrow agreement was worked out

(Testimony of Harry C. Kendall.)

and executed by the Board of Directors, Step 4, Exhibit D?

A. And the other parties involved.

Q. Yes; an escrow agreement was worked out, and then the Board of Directors instructed its President to execute the escrow, Step 5, didn't they, as you recall?

A. Well, I can't say that I recall it. All I can do is read the book here and assume.

Q. You will accept that, what is in the book, as correct; do you not?

A. No, I do not, because a lot of it is absolutely incorrect.

Q. Because it shows these Trust Certificates as corporate liability; is that one? [61]

A. That's one.

Q. Because it suggests that Building Syndicate was buying this property; is that another?

A. That's correct; that is another that is incorrect. Both of those are incorrect.

Q. Could you suggest at this time, sir, then, why the income tax returns, if it should later develop were returned on the basis that Building Syndicate owned this property that the Trust Certificates were liabilities, would you have an explanation at this time?

A. No, I——

Q. All right; if it should later——

A. But that was prepared by an accountant, and I probably never even saw that.

Q. If it should develop by subsequent evidence, Mr. Kendall, that the annual reports of your cer-

(Testimony of Harry C. Kendall.)

tified public accountants, which included three different ones—there were three different ones; you recall that, sir—

A. Yes.

Q. —should all show this land as being owned by Building Syndicate and these Trust Certificates as liabilities, would you have an explanation for that, sir, at this time?

A. Yes.

Q. Which would be—

A. The fact that the bookkeeper or accountant or whoever it [62] was originally set it up probably wanted to show all the money involved in this escrow deal, and, being familiar with that Land Trust Certificate or this kind of a deal, it probably showed the amount of money received from the sale of Land Trust Certificates as though it were an indebtedness, which, of course, it was not. The facts absolutely show, and it is just perfectly apparent, that these documents and these returns are totally contrary to the facts.

Q. Who is Mr. A. R. Watzek, Mr. Kendall?

A. He is a local gentleman.

Q. What was his connection with Building Syndicate?

A. He was President of it.

Q. And E. J. Chase?

A. He was a bookkeeper, I believe, with Strong & MacNaughton Trust Company.

Q. Was he not Assistant Secretary of Building Syndicate?

A. The records show that he was. I had forgotten that he ever was. I have never even met the gentleman.

(Testimony of Harry C. Kendall.)

Q. Peat, Marwick, Mitchell & Co. has been the auditor for a number of years? A. Yes.

Q. And I. D. Wood & Co.? A. Yes.

Q. And that is since Mr. Tourtellotte, a certified public accountant by the name of Arch [63] Tourtellotte? A. Yes.

Q. Do I understand your testimony to be, Mr. Kendall, that all of these men and all of these documents, including the minutes of your own Board of Directors meetings, are mistaken in your view?

A. Yes.

Q. Is there anybody else living or any other documentary evidence available which you have now, sir, which would support your view?

A. Yes.

Q. Yes?

A. Well, A. R. Watzek, for instance, President of the company, he never had any idea that we owned this property or that we had had a liability—or mortgage or anything of the sort. I never even dreamed of anything like this until this tax case came up. Nobody ever assumed it was a mortgage. Nobody ever assumed we owned the property. At the time of the negotiations with Union Trust Company we assumed they could cancel our lease on 60 days' notice, and on one occasion we got down on our knees and begged them to give us time. We didn't think we had any year's time of redemption. We had none of the prerogatives of a mortgagor.

Q. Moving back to 1927, the corporation was named and the pursuits which are here. What the

(Testimony of Harry C. Kendall.)

parties were trying to do, as you know, Mr. Kendall, was simply to get enough money to pay [64] for the building for which it had an option?

A. No.

Q. And the Land Certificates?

A. We never intended to buy the building. We never had any possibility of buying the building. We couldn't raise enough money to buy the building. The only thing we hoped to have was a leasehold.

Mr. Biggins: That is all, Mr. Kendall.

Redirect Examination

By Mr. Stoel:

Q. Mr. Kendall, there has been a good deal of reference here to minutes and the characterization of this transaction in the minutes. I do not have a copy of the minutes directly in front of me, but I think I can broadly characterize the areas that Mr. Biggins has been discussing here. I think you have just read here frequent references in these minutes to the purchase of this property by Building Syndicate, and I think other places refer to acquisition of the property by Building Syndicate.

You have testified, I think, in your final answer here that you understood that all you were getting was a leasehold. Now, what was the term of that leasehold, Mr. Kendall?

A. A 99-year lease with the privilege of extensions and an option to buy for \$1,417,500. [65]

Q. Did you understand that under that lease

(Testimony of Harry C. Kendall.)

that you have the right to occupy the building during the entire time of the lease, talking in general terms, for 99 years? A. Yes.

Q. As long as you didn't default?

A. Yes.

Q. Did you understand that if you could raise the money to exercise the option, that you might some time acquire the entire property?

A. Yes.

Q. During the period that you might be occupying the property as a lessee, would you have complete control of the premises as far as the rental policies, retaining the net profits of the company for yourself, the lessee, excluding people from the building, most of the rights that go with—are thought to go with ownership? A. Yes.

Q. And to put in a layman's view of the transaction, then, any referring to the minutes of showing no references in the minutes to the acquisition or purchase of the Northwestern Bank Building property—

Mr. Biggins: I am going to object to further leading questions, your Honor.

The Court: The question is leading. Sustained.

Q. (By Mr. Stoel): You have been asked again—let me go [66] back and ask you in the term Mr. Biggins asked it, perhaps. These minutes refer to purchase of property and the acquisition of the property, and will you state your answer again as to what you thought you were acquiring?

A. A leasehold.

(Testimony of Harry C. Kendall.)

Q. Is that the word used, I think, normally through these minutes to Northwestern Bank Building property? You have got the incidents of ownership that you understood were a part of that leasehold interest that you have such as possession, control, and so forth; is that right? A. Yes.

Q. So that in referring to the purchase of the property and in saying that you understood the purchase was a leasehold, is it fair to say that what you had in mind was the acquisition of these interests incident to a leasehold?

A. Yes; in referring to this as ownership of the property, you might compare it to a man who is in possession of a house that belongs to his father, and his father is in a rest home and going to die, and he is going to inherit the house. He would be very likely to refer to that house as his house. He lives in it; he knows he is going to own it or hopes he is going to own it. We were living in his house, and we hoped that some day we would own it, but for twelve years it looked as if we couldn't even retain possession of it without getting a concession from the Trustee for the Land Trust Certificate owners [67] whom we knew could cancel our lease on 60 days' notice and throw us out, and we acted accordingly, and everybody acted accordingly, and nobody ever suggested that we had any rights of redemption or could defend ourselves in any way.

In fact, when one of our officers got a little tough on the deal, the Trustee immediately proceeded to

(Testimony of Harry C. Kendall.)

take steps to cancel the lease, and I remember very well that incident where I persuaded that gentleman to give us a little more time, and we were doing our darndest to work it out for twelve years when we were practically, well, over ten years when we were unable to pay our lease requirement even.

Q. In the negotiations which have been reviewed with you by Mr. Biggins leading up to the final escrow agreement, Building Syndicate was a corporation staffed by local people, was it not?

A. Yes.

Q. They were interested, you have said, in acquiring a leasehold in this property with an option to purchase?

A. Yes.

Q. I think that you have also said that that was **all that you could see your way free to or be able to finance at that time**, was the acquisition of that leasehold and option to purchase?

A. It was utterly impossible to finance a first and second mortgage. In the first place, Lumbermens Trust Company would not underwrite the second mortgage issue, and, in the second [68] place, the first mortgage would require about 5 per cent interest plus about 5 per cent payments on principal, which would be 10 per cent on what was \$1,350,000, \$135,000. There wouldn't be anything left for anybody. That would have taken all the income there was there.

Q. Because you saw this as a—you and your group, Building Syndicate, saw a feasible way to acquire an interest in the property for the kind of

(Testimony of Harry C. Kendall.)

investment that you could make, is it fair to say that you were interested in pushing the deal to a conclusion?

A. Certainly, and we were all interested in getting possession of what we hoped could be made into a valuable income-producing property with a very small investment. The only possible way to do that was through a leasehold.

Q. So that because of this interest in pushing the matter to a conclusion, you would have taken an active role——

The Court: Mr. Stoel, your questions are very, very leading.

Q. (By Mr. Stoel): Did you take an active role, then, in Building Syndicate in the pressing of this matter to a conclusion after the August formation of Building Syndicate?

A. Yes, I definitely did, even to getting out of my role as a buyer and becoming a salesman traveling all across the country to sell the leasehold bonds.

Q. Was it necessary that the other two parties to this [69] transaction, two principal parties, namely Union Trust Company and Lumbermens Trust Company, that their agreement be obtained to the proposal for closing this transaction?

A. Yes.

Q. Why was that necessary?

A. Because they were putting up the money, all except the \$300,000 of stock.

Q. Did, then, all three of the parties—Building Syndicate, Union Trust and Lumbermens Trust—

(Testimony of Harry C. Kendall.)

participate, each representing its own part of the transaction in the formation of the escrow agreement? A. Yes.

Mr. Biggins: That calls for a conclusion, your Honor.

The Witness: I have stated it already.

The Court: It does call for a conclusion. The instruments are the best evidence.

The Witness: I think I have stated that several times in the testimony.

Mr. Stoel: I think that is all, your Honor.

Recross-Examination

By Mr. Biggins:

Q. Just one question on surrebuttal, Mr. Kendall. I think you said Lumbermens Trust would not give you a second mortgage on this property. Did you testify to that? [70]

A. That we were not undertaking to market a second mortgage.

Q. So the inquiry was made? So such an inquiry was made of Lumbermens Trust? A. No.

Q. Well, how do you know they would not market it for you, Mr. Kendall?

A. Because I was buyer for them, and my business was setting up bond issues. I knew we would not go out and try to sell second mortgage bonds. It was bad enough to sell the first mortgage leasehold bonds, and we had considerable difficulty in doing that.

(Testimony of Harry C. Kendall.)

Q. So that was the reason we finally had to resort to this financing arrangement, wasn't it?

A. There was never any question—I knew the moment this was put up to me by Black that the setup he had was the only practical way that I could play any part in this deal. I didn't have to analyze it.

Q. And the very words, I submit, Mr. Kendall, the very words you used with Mr. Black were that, "We could purchase this property"? Now, honestly, those were the words used, weren't they?

A. Well——

Q. Those words back there when you were talking to George Black, "It is the only way we can buy this property"; that's what you said, now, wasn't it? [71]

A. We never did buy it.

Q. But that's what you said?

A. All right, now, there is just an example of loose use of words. Maybe I did say that, but you know what I meant, acquire possession of this property to get the benefits from the rent.

Q. Thank you, Mr. Kendall.

A. I am just not a lawyer, and I am not a writer, so perhaps I don't use exactly the right word at the right time.

Mr. Stoel: That is all I have.

The Court: You may step down, Mr. Kendall. We will have our noon recess until 1:30, 1:30 this afternoon.

(Noon recess taken.) [72]

Afternoon Session

(Proceedings herein were resumed at 1:30 p.m. of the same day, pursuant to the noon recess, as follows:)

The Court: You may proceed, Mr. Stoel.

Mr. Hayhurst: We will call Mr. Coney.

AMIS C. CONEY

a witness produced in behalf of the plaintiff, having been first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Hayhurst:

Q. Will you state your address, please, Mr. Coney? A. Pittsburgh, Pennsylvania.

Q. What is your present occupation, Mr. Coney?

A. I am a general partner of a New York Stock Exchange firm in Pittsburgh by the name of A. E. Masten & Company.

Q. What is the address of that company, please?

A. First National Bank Building, Pittsburgh.

Q. Mr. Coney, have you had considerable background in the investment business?

A. Yes, all my life.

Q. Would you please describe your background?

A. I finished college in 1909, and I went into the investment [73] banking business with William A. Read & Company of New York, now Dillon, Read & Company, and for about twelve years I had an office in Rochester, New York, and handled the busi-

(Testimony of Amis C. Coney.)

ness out of all Western New York from Syracuse to Buffalo.

Then I went from there to the Union Trust Company of Cleveland, and I had charge of investigating and underwriting the purchasing of securities of different kinds.

Q. In what year did you go with the Union Trust Company, please? A. 1921.

Q. Were you with the Union Trust Company in 1927? A. Yes.

Q. In what capacity?

A. Well, the capacity that I just spoke of, and my title was Vice-President.

Q. Were you with the Bond Department of Union Trust Company at that time? A. Yes.

Q. Could you please tell us what the function of a Bond Department was in Union Trust Company at that time?

A. Well, the function of a Bond Department of that bank, and I think most other banks that had Bond Departments, was to take care of investment business in all its phases that was done with the customers of the bank; in other words, as distinct from managing the bank's own portfolio. That included the underwriting [74] and purchase, distribution of all kinds of investments except common stocks. We were not permitted to deal in common stocks by the Ohio laws and by the Federal Reserve regulations.

Q. Mr. Coney, in 1927 did you have occasion to become familiar with a transaction involving the

(Testimony of Amis C. Coney.)

Northwestern National Bank property in Portland, Oregon? A. Yes.

Q. Did you participate in that transaction?

A. Yes, I did.

Q. In whose behalf did you participate?

A. The Union Trust Company.

Q. Mr. Coney, what was the policy of the Union Trust Company at that time in relation to Land Trust Certificate transactions?

A. Well, we were empowered to, and did also, deal in that form of investment. The policy was to buy the plan, take title to it in trust capacity, and issue certificates of equitable ownership and sell them.

Q. Was Union Trust Company at that time actively seeking out properties to buy for this purpose? A. Yes, if we felt they were good.

Q. Mr. Coney, apart from this transaction in Portland, Oregon, involving the Northwestern Bank Building, to your knowledge had this form of transaction ever been used in Oregon before?

A. I never heard of it on a public transaction, and I think I would have heard if it had been. [75]

Q. Mr. Coney, how was this particular transaction involving the Northwestern Bank property brought to your attention?

A. An investment firm in Cleveland, George W. York & Co., called it to our attention.

Q. To the best of your recollection, Mr. Coney, what was the stage of the transaction at the time it was called to your attention?

(Testimony of Amis C. Coney.)

A. An agent named George Black had called it to the attention of George York & Company, and George York & Co. had made a preliminary investigation, brought it to us, said that Mr. Black had an option on the property here, the building of a defunct bank, the Northwestern Bank, and asked us if we would like to investigate it further with the idea of ultimate issuance of Land Trust Certificates for their distribution.

Q. Mr. Bailiff, would you please hand the witness Plaintiff's Exhibit 1?

(Document presented to the witness.)

Q. Mr. Coney, will you please examine Plaintiff's Exhibit 1 and then state to the best of your recollection whether or not that document was in existence or had been received or issued by George W. York & Co. at the time that you were called into the transaction? A. Yes; yes, indeed.

Q. Did you then make an investigation of the Northwestern National Bank property? [76]

A. Yes, I investigated it personally and also got our officer in the bank building interested, which, incidentally, then was said to be the largest bank building or commercial building in the world—a very able man, to come out here and go over it, verify the values and the operations, and on his favorable report I came out here.

Q. Mr. Coney, after the Union Trust Company came into the picture what happened to George W.

(Testimony of Amis C. Coney.)

York & Company? What part did they then play in the transaction?

A. Well, it became joint underwriters, minor underwriters, but after we had purchased the issue of Land Trust Certificates we syndicated them, which means we interested other dealers in buying and distributing them, and York was one of those dealers. I don't remember on what scale.

Q. Mr. Coney, what was the situation of the Northwestern National Bank of Portland at this time?

A. We were told it was in liquidation.

Q. To your knowledge, Mr. Coney, was the Northwestern National Bank of Portland affiliated in any way with the Union Trust Company of Cleveland?

A. No.

Q. In this transaction, Mr. Coney, what role was played by the Union Trust Company of Cleveland?

A. Well, first we investigated the property and, as I told you before, tried to make sure that it gave a sound basis for [77] the purchase of the real estate and distribution of certificates; and, second, we negotiated for the purchase of the property on terms substantially like those that are set forth in this letter from Mr. Black to George York & Company.

Q. Did Union Trust Company in connection with this transaction sell certificates of beneficial ownership in the property to investors, to the public?

A. Yes.

Q. Would the Bailiff please hand Plaintiff's Exhibit 3 to the witness?

(Testimony of Amis C. Coney.)

(Exhibit presented to the witness.)

Q. Mr. Coney, do you recognize the document marked as Plaintiff's Exhibit 3? A. Yes.

Q. Was that document prepared by yourself?

A. It was prepared by my department, and I had a good deal to do with it; yes, sir.

Q. Was Plaintiff's Exhibit 3, or, of course, counterparts of that exhibit, used by the Union Trust Company in marketing Land Trust Certificates to the public? A. Yes.

Q. Of course, those were certificates of beneficial interest in the Northwestern National Bank property that we have been talking about?

A. Yes. [78]

Q. Mr. Coney, what was the transaction between Building Syndicate and Union Trust Company?

A. Building Syndicate was a corporation, a new corporation, which entered into a 99-year lease with the Union Trust and the Security Savings & Trust as owners of the fee.

Q. I think we have not mentioned that before. What was the role played in this transaction by Security Savings & Trust Company of Portland, Oregon?

A. It was a Co-Trustee since a Cleveland banking institution was not permitted to hold real estate outside of the State of Ohio.

Q. Has that been the reason why the Security Savings & Trust Company was associated by the Union Trust Company in this transaction?

(Testimony of Amis C. Coney.)

A. Yes.

Q. Would you continue, then, please, to describe the relation or the transaction between Building Syndicate and Union Trust Company?

A. I beg your pardon?

Q. I say, would you please continue with your description of the transaction between Building Syndicate and Union Trust Company?

A. Well, as we proposed to be the owners of the fee, we had the job of negotiating a long-time lease with all of its provisions with the corporation that was to be the lessee corporation, [79] and that was our principal negotiation.

Q. In this particular transaction who was to be the lessee corporation?

A. Building Syndicate.

Q. Mr. Coney, what was the transaction, if you know, between Building Syndicate, having established a leasehold estate, planned to mortgage that estate and issue leasehold bonds against it which were to be sold to the Lumbermens Trust Company? Did you personally, Mr. Coney, participate in any negotiations with Building Syndicate concerning the terms of lease from Union Trust Company to it?

A. Oh, yes.

Q. Do you recall who the persons were with whom you dealt in those negotiations?

A. Well, I think principally with Mr. Robert Strong of Strong & MacNaughton Trust Company and occasionally with Mr. Kendall who is here, and

(Testimony of Amis C. Coney.)

with Mr. Hampson of Dey, Hampson & Nelson, their attorneys.

Q. Do you recall any of the subjects of those negotiations?

A. Well, in a long-time lease there are many provisions that had to be agreed upon by both lessor and lessee, such as, for example, default provisions, covenants, agreements to maintain property and to pay the taxes, and so forth.

Q. With regard to the negotiations on the default provisions, Mr. Coney, was it ever suggested or discussed in those [80] negotiations that the lessor would be compelled to bring an action in court in order to terminate the interest of Building Syndicate?

A. No, this was an outright ownership and a lease of 60 days' notice to the Trustee representing the Land Trust holders, terminating the lease.

Q. Was there in those negotiations ever any discussion or mention that Building Syndicate would have a period of time following default and termination of the lease in which it could redeem its interest in the property?

A. No, none whatsoever.

Q. Mr. Coney, what interest in this property did Union Trust Company acquire in this transaction?

A. The whole fee.

Q. Was this fee acquired by Union Trust Company only as a security interest for the debt of Building Syndicate?

A. No, there was no debt.

(Testimony of Amis C. Coney.)

Q. Mr. Coney, in this transaction, to the best of your knowledge, did Building Syndicate ever apply to Union Trust Company for a loan on this property? A. No.

Q. Did anyone else ever apply for such a loan in behalf of Building Syndicate?

A. No, not to my knowledge.

Q. Was a loan ever offered to Building Syndicate by Union [81] Trust Company on this property? A. No.

Q. In the various negotiations in which you participated, was there ever any discussion of a loan on this property of Union Trust Company?

A. No.

Q. Mr. Coney, at any time around the time of this transaction, or prior thereto, was Building Syndicate to be indebted to Union Trust Company?

A. No.

Q. As a part of the negotiations in which you participated, Mr. Coney, was there ever any agreement or discussion that Building Syndicate was required to exercise its option to purchase the property? A. No, it was a pure option.

Q. I want you to understand that I am speaking now of an option given by Union Trust Company to Building Syndicate. A. Right.

Q. During these negotiations and the periods surrounding the closing of the transaction, was there ever any mention or discussion that the fee in the property was being taken by Union Trust Company only as security? A. No.

(Testimony of Amis C. Coney.)

Q. Mr. Coney, as a result of your experience in the investment business, are you familiar with mortgage financing? [82]

A. Yes, I have done mortgage financing.

Q. Is it part of your experience that ordinarily a mortgagor has the right to redeem the property after a default by paying off the indebtedness and making up the default? A. Yes.

Q. Was there ever any suggestion in any of these negotiations that Building Syndicate would have such a right with respect to the interest which it held under the lease from Union Trust Company?

A. No, indeed.

Q. Mr. Coney, in 1927 would you have recommended to the Union Trust Company that they make a loan of \$1,250,000 on this particular property in this transaction? A. No, I would not.

Q. In your opinion, Mr. Coney, would any other responsible lender have made such a loan on this property?

Mr. Biggins: I object to that question.

The Court: Sustained.

Q. (By Mr. Hayhurst): Mr. Coney, can you state whether or not the Land Trust Certificate was regarded as a popular investment by investors in Ohio in 1927? A. Yes, it was very popular.

Q. Can you describe the reasons for that popularity?

A. Yes, I think I can. In the first place, most of them were really good investments. They were, they involved the ownership [83] of good property

(Testimony of Amis C. Coney.)

with adequate improvements. The record was excellent and has been even through the depression. Also, we had at that time an extremely high personal property tax in Ohio which was very onerous and made the ownership of fixed income securities rather hazardous, and these being, of course, not securities but interests in land, were not subject to personal property tax since the real estate taxes were paid by the lessee under the terms of the lease.

Mr. Hayhurst: That concludes our direct examination, your Honor.

The Court: Mr. Biggins?

Cross-Examination

By Mr. Biggins:

Q. May it please the Court. Mr. Coney, I believe you said you had one of the best experts in the business go out to appraise this property?

A. No, I didn't say that at all.

Q. Somebody came out to appraise; is that right?

A. Somebody came out to examine it and see if it was suitable property for us to buy for this purpose, yes.

Q. I believe you testified, Mr. Coney, that you were familiar with the commitment that George Black had with the George York Company. You looked at Exhibit 1?

A. At the letter, yes. [84]

Q. All right. Now, after the commitment, Exhibit 1, was made, Union Trust Company made a second and different commitment with Building Syndicate, did they not?

A. Yes.

(Testimony of Amis C. Coney.)

Q. Now, in that second commitment—by the way, do you know whatever happened to any copies of it? Do you have a copy of it? A. No.

Q. Do you know what happened to it?

A. No.

Q. When you made that commitment, it was on the written understanding that the property had to meet a certain appraised value; was it not?

A. I don't recall any such thing, no.

Q. It was common in the Union Trust Company in inviting and underwriting, if you will, the land fee certificates to require a minimum appraisal on the property, was it not?

A. I don't believe that was a pre-condition requirement, no.

Q. If this property were appraised by an independent appraisal expert, Mr. Coney, as \$1,350,000, would your company issue a fee land certificate on the total amount?

A. Well, it depends on who appraised it.

Q. Exactly, sir; and an appraisal would have to be made, wouldn't it?

A. No; in answering your question, we would not make any [85] commitment on an appraisal we didn't see.

Q. May I see Exhibit 1, please? Looking at Page 3 of Exhibit 1, Mr. Coney, it says in the second paragraph down,

“You will supply us with——”

Will you notice that language, please——

“You will supply us with——”

(Testimony of Amis C. Coney.)

Would you read it, sir?

A. Yes, I have read that.

Q. "You will supply us with all necessary description of the property, pictures of building and appraisals——"

Now, would you read that into the record, appraisals of what?

A. "——and appraisals of both land and building by responsible appraisers of the City of Portland, acceptable to us."

Q. And continuing?

A. "Such appraisals shall show a valuation of the land of not less than \$1,370,000 and a valuation of the building of not less than \$1,350,000."

Q. Was it customary to make such a requirement in making a commitment under a fee certificate issue as this appraisal?

A. Well, it was sometimes done and sometimes not.

Q. But Union Trust did in this case, sir?

A. In this instance Union Trust, they say——

Q. Could I have Exhibit 3, please? [86]

(Document produced.)

Q. That is a prospectus. Would you examine it? That is the Union Trust prospectus now, isn't it, Mr. Coney? A. Yes.

Q. Which was sent by Union Trust to Building Syndicate for their approval? A. Yes.

Q. Later issued and published by your company to the investing public? A. Yes.

(Testimony of Amis C. Coney.)

Q. Included in which, under the style, "Valuations," about the middle of the page, it says,

"The land owned in fee has been appraised by Mr. Philip V. W. Fry of Portland, Oregon,"

at how much? A. \$1,400,000.

Q. And for the building?

A. And the building, \$1,384,000.

Q. And the total as indicated in your prospectus is \$2,784,000; right? A. Yes.

Q. Why was that valuation appraisal put in your prospectus, Mr. Coney?

A. Well, because the purchaser of a Land Trust Certificate is entitled to know what appraisers and others think of the value [87] of the property that is being transferred to him in equitable ownership form.

Q. Knowing that and knowing that and making recommendations on this issue, your company sought and secured information as to this appraisal, didn't they? A. Yes.

Q. If this appraisal had been less than two million dollars, would your company have underwritten this issue?

Mr. Hayhurst: I object to that as speculative, your Honor.

The Court: It is properly cross-examination.

The Witness: I haven't any idea.

Q. (By Mr. Biggins): They would have to take a second look at it, wouldn't they?

A. I haven't any idea what would have been done.

(Testimony of Amis C. Coney.)

Q. You were the supervisor of what department for Union Trust?

A. I was in charge of the underwriting and purchasing and, to some extent, distribution of securities, although we had a sales manager for it.

Q. Which was called the Bond Department, I think? A. Yes.

Q. In Ohio your bank made mortgage loans on satisfactory security; did they not?

A. Yes.

Q. But in Ohio your bank did not successfully float mortgage bond issues, did they? [88]

A. Yes, they did.

Q. Are you familiar with Mr. B. G. Huntington, President of Huntington National Bank of Columbus?

A. I knew him in his lifetime—which Huntington?

Q. B. G. Huntington, President of the Huntington National Bank of Columbus, Ohio.

A. Well, I have met the gentleman years and years ago, yes.

Q. Would you have agreed with his statement on the condition of the market in Ohio that many of these—

Mr. Hayhurst: Will you clarify this as to the time, please?

Mr. Biggins: Well, it is some time that we are at in the Lazarus case. I believe that loan was dated around 1926, 1927, 1928, right around in that area, where he stated that in many of these financing

(Testimony of Amis C. Coney.)

arrangements that they negotiated in the form of Land Trust Certificates because this is all almost the only possible plan because of local—meaning Ohio—taxation on mortgage bonds. Would you agree with that statement? A. No.

Q. But many members of the financial community in Ohio at that time did hold such an opinion; did they not?

A. I don't know. There were many, many taxable bond issues floated in Ohio at that time.

Q. Which were, if I use the word "sticky," and, as a financial man, you know what I mean, don't you? Sticky, a sticky market? [89]

A. I know what you mean, but you are wrong in your conclusion.

Q. The market on mortgage bond issues was sticky in Ohio at this time?

A. I don't know.

Q. The market in the certificate fee issues, you will accept that as a common language in handling your loans?

A. Land Trust Certificates is the term we use.

Q. Land Trust Certificate, the Land Trust Certificate market was easier in Ohio at this time, but would you finance real estate undertakings because of the absence of the local personal property tax on that?

A. It was not invariable. It was not even general. It depended entirely on the facts of the case.

Q. And the facts of the case depended on the value of the underlying building, the value and security of the underlying building?

(Testimony of Amis C. Coney.)

A. And a hundred other considerations.

Q. Value and the security, sir, of the underlying building?

Mr. Hayhurst: I think he has answered that question, Counsel.

Mr. Biggins: No, he has not.

The Witness: Many other considerations.

Q. (By Mr. Biggins): You hesitate to say Yes, sir?

The Court: Can you answer that Yes or No?

The Witness: I don't think I can, your [90] Honor.

The Court: If you cannot, that is final.

Q. (By Mr. Biggins): At no time did Union Trust Company have an option to purchase this property from Northwestern, did they? At no time did they have that option? A. Well——

Q. Strike the question.

You knew there was an option some place to buy this property for \$2,200,000; you knew that, didn't you?

A. Well, I knew it was in the letter that you just showed me from George Black to York.

Q. And you knew that this option was going to be sold for more than was being raised by the Land Certificate issues; you knew that?

A. Well, at what point? After it was all over I knew it, of course.

Q. Let's look at Exhibit 3 again, Mr. Coney. Is that still before you? A. Which is that?

Q. Exhibit 3, sir; the prospectus, sir.

(Testimony of Amis C. Coney.)

A. Yes.

Q. Look down there where it says investment or security, I am not sure which. Is there not a reference to the fact that there is an investment of \$750,000 in leasehold mortgage bonds after the Land Certificates? Isn't that reference there in that prospectus? [91]

A. It says, "The investment in the leasehold estate is evidenced by an issue of \$750,000 First Mortgage Leasehold Bonds, and a large cash investment in common stock of the Lessee corporation."

Q. Which, from an investor's point of view, indicated the safety factor in this investment, did it not?

A. Well, it indicated a safety factor, yes.

Q. And the Land Trust Certificates were regarded, to use financial language, as priming the leasehold mortgage bonds?

A. I don't know what you mean by priming. I never heard that word before.

Q. May I ask you this way, then, sir: Have the leasehold bonds underwritten by Lumbermens Trust Company had a security lien prior to that of the Land Certificates underwritten by your company?

A. Prior to that?

Q. Yes, sir. You knew that they owed—

A. I just don't understand your question at all, leasehold bonds having security.

Q. Let's look at the money that went into this, Mr. Coney. \$750,000 came out of the bonds; you knew that?

(Testimony of Amis C. Coney.)

A. Yes—I didn't, nothing like \$750,000 came out.

Q. What did you say in your prospectus?

A. It said it is evidenced by the issue of \$750,000 that was paid for the issue. [92]

Q. But you didn't tell that to the people you sold those to?

A. Well, this was evident.

Q. Yes, \$650,000, is that the closing—

A. Six hundred seventy I think is the figure. I am not sure.

Q. The Land Trust Certificates, the actual sales price was \$250,000?

A. That isn't the sales price. That is the purchase price.

Q. Didn't you sell—yes, that's right, \$350,000?

A. No, that isn't it either, 1,350 equal, undivided shares was sold at \$1,010 for each of those shares. That was the sales price.

Q. To yield 5.44, but the face of the Land Certificates themselves—

A. There was no face. You cannot have a face of a thing other than evidence of ownership.

Q. A printed piece of paper went out, didn't it, Land Trust Certificate? A. Yes.

Q. On the face of those certificates was the amount, a thousand and how much—a thousand dollars, wasn't it?

A. No, 1,350 equal, undivided shares, but there is no figure of \$1,350,000 in any of the literature.

Q. To my question, though, Mr. Coney, you knew

(Testimony of Amis C. Coney.)

they were going to have to pay this money to the bondholders——

Mr. Hayhurst: What is this now, Counsel? [93]

Q. Indicating on a blackboard \$670,000, that was furnished through Lumbermens Trust Company financing, and you knew those had to be paid, didn't you? A. Had to be paid?

Q. Yes.

A. Well, what compulsion was there for anybody to pay it? At what point were we supposed to know that?

Q. Let's take it as a hypothetical question, and being an expert in the financial field, Mr. Coney—let's assume that there was a bond issue for \$670,000 by Building Syndicate. Let's assume that. Would it be material to your consideration in issuing this Land Certificate issue whether or not there was an obligation on the part of Building Syndicate to pay these bonds before they paid you, the holder of the Land Certificates?

A. Not necessarily, because they could all have been in stock, or it could have been in any other form.

Q. If it was in the form of bonds, sir, and payment on those bonds came before the payment of the rent, would that have been significant in considering the underwriting of this issue?

A. I don't understand the conditions you are citing in which payment on the leasehold bonds would be prior to the payment of rent.

Q. Let's skip to the blackboard then. In financ-

(Testimony of Amis C. Coney.)

ing a corporation there are varieties of equitable capital furnished; are there not? [94]

A. Sometimes.

Q. Pardon? A. Sometimes.

Q. There is common stock?

A. Well, if it's a stock——

Q. That is easy, isn't it, Mr. Coney? There is common stock?

A. There usually is common stock.

Q. Preferred stock there can be?

A. Well, I know one of your largest companies right here in Portland that doesn't have any common stock. I mean, if you are trying to pin me down, the Great Northern Railroad has no common stock.

Q. Are you familiar with financial arrangements that are commonly made with corporations?

A. I have some knowledge of it.

Q. Generally speaking, there is common stock?

A. Generally speaking, if you put that in, I would say Yes.

Q. And preferred stock?

A. Maybe sometimes.

Q. Sometimes, and secured bonds; secured bonds?

A. Sometimes.

Q. Indentures?

A. Sometimes——indentures, there isn't any such thing as a security called an indenture. An indenture is a deed of trust.

Q. Debenture. I used the wrong word— [95]
debenture.

(Testimony of Amis C. Coney.)

A. Yes; there can be debentures, yes.

Q. In arranging, in general terms, Mr. Coney, on the financing of a corporation, is it important to the senior bondholders whether or not the debenture payment comes before or after the security of the prime bonds, as a general proposition in arranging corporate finances?

A. I never heard of a case in which an unsecured debenture is paid until the first mortgage is paid.

Q. Exactly, the first mortgage bonds look for the security of the property itself? A. No.

Q. What do they look for their security on?

A. Well, the property itself only in foreclosure.

Q. The payment being expected out of the income that is earned from the property?

A. Well, that is very different, yes.

Q. And being paid prior to the payments made to junior debenture holders?

A. Well, as a rule, but not always even there.

Q. It is something considered in floating the prime bond issue, isn't it?

A. Well, what is the something considered in this?

Q. A security of investment, and answer it this way, if we may, then: Would there be a difference in interest rate paid between a secured bond and an unsecured debenture? [96]

A. Might be——

Q. On the same corporation at the same time?

A. No; it might be very different. One type of debenture might get a much lower rate, and I fre-

(Testimony of Amis C. Coney.)

quently have seen it. It might have a much earlier maturity, for example. It might be convertible. There are lots of conditions in which a debenture would get a lower rate than a mortgage bond.

Q. Just one final question, Mr. Coney. You say your appraisal there came out to \$2,784,000 on this prospectus?

A. Well, the appraisals of these two gentlemen who are quoted here, yes.

Q. I am asking you whether under Ohio law and under the policy of your bank of which you are Supervisor in the Bond Department—

Mr. Hayhurst: I object to this question, your Honor, as far as it relates to Ohio law. This man is no expert on that.

Q. (By Mr. Biggins): Under the scope of your authority as Supervisor of the Bond Department of the Union Trust, I am asking you, sir, could you have underwritten the full Land Certificate issue to the full amount of the appraisal price? Your answer is No, isn't it?

A. No; I don't know whether it is or not.

Q. Would you have recommended it, Mr. Coney?

A. Oh, I can't reconstruct all the factors at this time to decide whether we would or not. I haven't any idea.

Q. Are you suggesting, sir, Mr. Coney, that as Supervisor [97] of one of the largest financial institutions in Cleveland that you are not at all certain whether or not you personally would recommend to your investing clients the full issue of

(Testimony of Amis C. Coney.)

Land Trust Certificates in the full amount of the appraisal price? You are not certain?

A. I am not suggesting anything.

Q. You would not have recommended that, and you know as a matter of policy of your bank they would not have permitted it either, would they?

A. I haven't any idea.

Mr. Biggins: That is all.

Mr. Hayhurst: If your Honor please, Mr. Fraser has pointed out one matter to me that perhaps should more properly have gone in on direct. I would like to clear it up right now.

The Court: You mean to open up your case?

Mr. Biggins: We have no objection.

Further Direct Examination

By Mr. Hayhurst:

Q. Mr. Coney, is the Union Trust Company still in existence? A. No.

Q. When did it go out of existence?

A. Well, it was closed by the RFC, the Federal Reserve Board, in 1933, and there was a liquidator and a conservator who kept the bank open—I mean kept the property as such, Union Trust [98] Company, for several years after that.

Q. Do you know who was the successor to Union Trust Company under the lease of Northwestern Bank property, to Building Syndicate?

A. Yes, the National City Bank of Cleveland.

Mr. Hayhurst: That is all.

(Testimony of Amis C. Coney.)

The Court: Mr. Coney, I would like to ask a question. Are these Land Trust Certificates still in use?

A. In Ohio? Well, I am sorry, in use, a great many of them are still outstanding, sir.

The Court: No; I mean new issues.

The Witness: The tax law was repealed in Ohio, and I have not seen any new issues of these for a good many years. I doubt if it is still in use.

The Court: In your institution you use this form of a certificate for the sale of lands or acted as trustees on more than one occasion?

The Witness: On many occasions.

The Court: On many occasions. Was the option clause in favor of the lessee always in the——

The Witness: Not always; no, sir. The earlier ones didn't have it, some of the earlier ones.

The Court: That is all. [99]

Cross-Examination

By Mr. Biggins:

Q. That raises a couple of questions. Didn't you think the option clause, Mr. Coney, always had a provision where the lessee could redeem those certificates, though; did they not? A. No.

Q. Any matter that your firm floated, one issue, sir, that they didn't have the option or right to redeem?

A. Now you used the word "always." I don't know anything about always.

Q. Can you think of a single instance where

(Testimony of Amis C. Coney.)

they didn't have one of two things, either the option to purchase the property or the right to redeem the certificates, that you know of?

A. Not that I know of where they had the right of redemption of the certificates. You cannot redeem.

Q. There is the right of redemption of certificates in this one trust agreement, is there not, on payment of a \$50 premium? A. No.

Q. You are not aware of that being in this agreement?

A. No; it is just simply the right to purchase property, in which case the trustee pays the certificate owners.

Q. In understanding the tax question in Ohio, Mr. Coney, there was a tax on mortgage bonds for awhile; is that correct? A. Yes.

Q. When that was repealed, the tax on mortgage bonds, you [100] know of no new issue of Land Trust Certificates, and that was your answer to the Court, wasn't it?

A. Well, I—yes; I don't know of any such now.

Q. And the companies went back to mortgage bonds, though of a similar arrangement?

A. No; I have not heard of any big mortgage bonds. The market for real estate securities in general with the public has almost completely disappeared since the Depression. There were numerous concerns in the business of setting up, issuing real estate bonds of all categories, but for at least ten

(Testimony of Amis C. Coney.)

years I do not recall a single such issue coming to the public.

I think public real estate financing has gone by the board. It has been done privately.

Mr. Biggins: Thank you, Mr. Coney.

(Witness excused.) [101]

WILLIAM L. BREWSTER

a witness produced in behalf of Plaintiff, having been first duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Stoel:

Q. What is your present occupation, Mr. Brewster?

A. I am a member of the firm of Brewster, Scholz & Burnett engaged in the property management business.

Q. Do you hold any office in plaintiff, Building Syndicate Co.?

A. I am the Secretary-Treasurer.

Q. How long has your firm been the—strike that—is your firm the building management firm which operates for the Building Syndicate Co. the American Bank Building? A. It is.

Q. Do you know what building management firms have occupied the same capacity for the plaintiff or its predecessor company since 1927?

A. Yes.

Q. Can you name those? First, start in 1927?

(Testimony of William L. Brewster.)

A. First, Strong & MacNaughton Trust Company; then its successor, the Commonwealth Trust & Title Company, I think the name was; then the management was transferred to Robert H. Strong who did business under the style of Robert H. Strong & Associates. After that it was handled by a successor partnership known as [102] Strong & Brewster, of which I was a member with Robert Strong, and then finally by Strong & Brewster, which was the business under which I did business as an individual, and finally under the partnership which is the present management; Brewster, Scholz & Burnett.

Q. Have you been employed by or a partner in all of the firms that you have mentioned?

A. Yes.

Q. During this period? A. Yes.

Q. Have you, as the Secretary-Treasurer, custody of the corporate records of Building Syndicate Co.? A. I do.

Q. And of the existing records of its predecessor company, Building Syndicate?

A. Yes; certain records as we have from the previous company.

Q. Have you searched those records, both those of the plaintiff and the predecessor company, for an escrow agreement which has been referred to as the closing agreement in the Northwestern Bank Building purchase? A. I have.

Q. Were you able to find it?

(Testimony of William L. Brewster.)

A. I was not. I have no record of ever having it in the company files.

Q. Did you also search the records for the document which is [103] referred to in the minutes as the trust commitment from Union Trust Company in 1927?

A. I likewise searched for that, and likewise I have no record of ever having received it from the previous managers.

Mr. Stoel: That is all.

Mr. Biggins: May it please the Court, as a preliminary inquiry, I will want to ask some questions on the books and records which I know would be improper cross at this time.

Mr. Stoel: Mr. Brewster can remain here, I think, if that is your question.

Mr. Biggins: Or do you want me to do it at this time for his convenience? I will do it either way.

Mr. Stoel: I think he is going to remain.

The Witness: I will be available.

Mr. Biggins: I have no questions at this time, then.

The Court: You may step down. Please remain here, Mr. Brewster.

(Witness temporarily excused.)

Mr. Stoel: Plaintiff rests, your Honor.

Mr. Biggins: May it please the Court, may I call Mr. Brewster as a hostile witness under the Rules?

The Court: You may. [104]

WILLIAM L. BREWSTER

was thereupon produced as an adverse witness in behalf of the Defendant and, having been previously duly sworn, was examined and testified as follows:

Direct Examination

By Mr. Biggins:

Q. I believe you said, Mr. Brewster, you are the custodian, corporate custodian of the books and records of Building Syndicate Co. and the prior company, the Building Syndicate? A. Yes.

Q. You recently made a search of these various books and records for certain documents?

A. I did.

Q. During the making of the search, did you even inquire or find out how Building Syndicate—that is, the old company—how Building Syndicate handled the purchase of this property on their books? A. No; I did not.

Q. Do you know to your own knowledge?

A. No, because I was——

Q. All right; I cannot ask you if you don't know.

Is your capacity both Secretary and Treasurer, sir?

A. Secretary-Treasurer for Building Syndicate Co.

Q. And, as Treasurer, are you familiar with elementary fundamentals of accounting?

A. I believe so. [105]

Q. Being familiar with elementary funda-

(Testimony of William L. Brewster.)

mentals of accounting, if a person purchased property, the usual accounting entry we would expect to find would be a debit to building and a credit to mortgage payable; is that right?

A. I didn't know any mortgage was involved here, sir.

Q. If we buy a building like the American National Bank Building on credit, part cash but mostly credit, what would be the entries you would expect to find on the books of the corporation?

A. Well, I think you would have us show a debit to the assets account and a credit to the source of the funds, whatever they might be.

Mr. Biggins: If it please the Court, could I ask the witness to examine—is this 5-foot-thick bundle that I have in my hand here, do you recognize this as being the general ledger of Building Syndicate?

A. Yes.

The Court: Is that marked as an exhibit?

Mr. Biggins: No; I have not marked any, and perhaps at this time, if the Court please, I have a whole group of documents to offer.

The Court: Are they marked?

Mr. Biggins: They are marked. We offer into evidence in this case the original income tax returns of Building Syndicate from 1927 through 1946. We didn't mark them in the pretrial exhibits, your Honor, because they were going to make objection, [106] as you recall.

The Court: I thought you were going to list

(Testimony of William L. Brewster.)

them, however. You did mention that yesterday afternoon.

Mr. Biggins: We will hand it over.

The Court: All right; we will want a list of these and then add it to the pretrial order. It will be amended so as to show it.

Mr. Biggins: I might offer Exhibit 50 for Identification, your Honor, the original income tax returns of Building Syndicate from 1927 to 1946.

The Court: What is that?

Mr. Biggins: I am making the offer so he can make the objection.

The Court: What are we offering, Mr. Biggins? We want to get this marked. What are you offering at the present time?

Mr. Biggins: I have the original income tax returns for all these years, 1927 through 1946.

The Court: Are you offering it as one exhibit or as individual—

Mr. Biggins: Yes, your Honor, they have already been marked, and they are catalogued there as A through R.

The Court: That is what I do not have, A through R.

The Clerk: No. 50, Exhibit No. 50, A to R, including R.

The Court: As I understand it, there is no objection to the authenticity of these? [107]

Mr. Stoel: Your Honor, there is no objection, if I may—

The Court: As to the authenticity.

(Testimony of William L. Brewster.)

Mr. Stoel: No, authenticity, no.

The Court: Now, then, you may have an objection at this time.

Mr. Stoel: Your Honor, I would like to inquire for what purpose defendant's counsel is offering these?

Mr. Biggins: As objective evidence of the intent and understanding of the parties, as evidence by their written jural act.

Mr. Stoel: I object to this, your Honor, on the ground that this is not any evidence of the intent of the second party to this transaction, the Union Trust Company, and that there is no showing that, if it is evidence of intent of Building Syndicate, that that intent was ever communicated to Union Trust Company.

The Court: Objection overruled. Exhibits 50-A through -R are admitted.

(Documents, income tax returns above referred to, previously marked Defendant's Exhibits 50-A through 50-R, inclusive, were thereupon received in evidence.)

Mr. Stoel: I should like to add to that the objection that the returns after 1928 are too remote to bear on the event, in any event. [108]

The Court: You may include that in your objection, and the objection is overruled.

Then you are offering No. S, now, I understand?

Mr. Biggins: Government now offers, your

(Testimony of William L. Brewster.)

Honor, what has been marked as Exhibit 51 for Identification, A through——

The Court: Just a moment. We have an S in evidence yet, 50-S. It was not included in the first offer.

Mr. Biggins: That was with the first group. I believe I said through 1946. I amend that to include 50-S.

The Court: 50-S will be considered as offered. Do you want the same objection?

Mr. Stoel: Yes, your Honor.

The Court: It will be received; same ruling; received.

(Document, income tax return above referred to, previously marked Defendant's Exhibit 50-S for Identification, was thereupon received in evidence.)

Mr. Biggins: The second group of documents, may it please the Court, are copies of Federal income tax returns from the files of Building Syndicate after 1927 through 1946, the same years, marked for identification 51-A through 51-Y, and offered.

Mr. Stoel: May I ask again what is the purpose of offering these returns, Mr. Biggins? Is there some definite purpose for offering these than that you gave as your first reason for offering the original returns? [109]

Mr. Biggins: There will be several, your Honor. The income tax for 1927, which is an exhibit marked

(Testimony of William L. Brewster.)

as 51-A for Identification, contains the original final closing agreement executed between the Secretary-Treasurer and the taxpayer, which we think bars them from changing the basis of depreciation. It contains the original, and with the other year's subsequent testimony, I believe, and the accounting records of the three C.P.A.'s that has been testified to so far, I will be able to show they knew of the existence of these prior returns, they had them available for examination and probably did examine them, and that consistently during this period from 1927 onward they treated Building Syndicate as the owner of this property and the Land Trust Certificates as corporate loans.

Mr. Stoel: Your Honor, so far as the admissibility of the returns of 1927, for the reason that he first gave, clearly the disclosure in that return of an agreement, the admissibility I would make no objection to, but admissibility of these returns for any other purpose I object to on the same grounds as the admissibility of the original returns and, in addition, I object on the ground that they are simply cumulative; that he has already put in what should be the best evidence of what the parties who filed the return thought was the proper return and that there is no purpose served by adding these. We are not questioning the authenticity of the original returns. I see [110] no reason why our retained copies offer any additional evidence in the case.

The Court: The objection is overruled. Received.

(Testimony of William L. Brewster.)

(Documents, income tax returns of Building Syndicate for 1927 through 1946, previously marked Defendant's Exhibits 51-A through 51-Y for Identification, were thereupon received in evidence.)

Mr. Biggins: I am not offering what has been marked for identification as Exhibit 3 at this time. I do not believe I need it, but, if the Court please, I am going to have a problem here. I do not want to offer this whole book. I do not think it is necessary. I would like to take numbered pages with the understanding any pages they might want in will be all right with me, too.

The Court: I agree that it is too voluminous to offer that entire exhibit, and if any part of it is admissible then I believe it should be the individual pages.

Mr. Stoel: With the understanding that there may be other portions that could be segregated out of there from our standpoint, we will work on that basis.

The Court: Certainly.

Mr. Stoel: We have not examined this in detail, so we are uncertain as to just what we might want to take out.

The Court: You may proceed, Mr. Biggins. [111]

Mr. Biggins: Well, I might offer No. 54.

The Court: No. 54 will be admitted as to those pages, unless you have an objection?

Mr. Stoel: Our objection to this goes to the same

(Testimony of William L. Brewster.)

point, your Honor, that there is no question of the authenticity of these documents now, but we do question their relevancy on the question of intent, and for the same reason that we objected to the original tax returns as not indicating that there was ever any communication of the intent whatever it may be, however it may be evidence here, to the Union Trust Company.

The Court: The objection is overruled. Now, if you would identify the individual pages, then, the whole number, then, starting with 54 through the alphabet, or starting with A, 54-A.

Mr. Biggins: That will be the unmarked journal pages appearing between Page J-26 and Page No. J-27.

Mr. Fraser: Your Honor, may I inquire whether we are starting to mark these 54 or 54-A?

The Court: 54-A, and then the next one in my thinking should be -B, -C, as to the pages that you actually offer that actually are received in evidence.

Mr. Biggins: Next, the unnumbered page styled within the group of ledger pages called Office Building Site, the third page over where it is written "Real Estate Parcel A" and the following page, "Leasehold Parcel B," and the third page— [112]

The Court: Are you marking those as you go through now, Mr. Biggins, so that we can get proper identification? That will be 54-B.

Mr. Biggins: The Leasehold Parcel B will be 54-C, which I am marking in pencil in the upper

(Testimony of William L. Brewster.)

right-hand corner in the blank space called Account Number, and the next one will be 54-D, which is written "Building, American Bank."

Turning over past the next slip called "Sinking Funds," the account which is numbered 75, I am marking for identification as 54-E, and it is styled, "Land Trust Certificates 1350 @ Call 1050, Interest Payable February 12th, August 1st (See Offset A/C 33)"; then after that "Interest 5½ Per cent."

And the following page, which I have marked 54-F, which is styled "Land Trust Certificates."

I offer exhibits marked for identification, your Honor, 54-A through 54-I, understanding that opposing counsel may include any other of these pages as he sees fit.

The Court: You were down to -F, I believe. Have you advanced to -I? I didn't get it.

Mr. Biggins: Yes.

Mr. Stoel: Your Honor, when he is finished offering these, I wonder if we can have a short recess where we could examine these pages he has designated now?

The Court: We will proceed now, Gentlemen, and then we can withhold the offer until such time as we have a recess. [113] We will have a recess in about half an hour.

Mr. Biggins: Could I ask the witness, if the Court please, to examine these documents that I have just made the offer on?

The Court: You have not had an opportunity to examine these?

(Testimony of William L. Brewster.)

Mr. Stoel: No; we have not examined these, your Honor.

The Court: We will have a ten-minute recess.

(Recess taken.)

Mr. Biggins: If the Court please, the Government offers into evidence exhibits marked for identification No. 52-A through 52-G, which are these annual reports of independent certified public accountants for the years 1927 through 1933, inclusive, marked -A through -G, which I believe is for the years 1927—excuse me, may I see that—yes, for the years 1927 through 1933 marked for identification as Exhibits 52-A through -G, inclusive.

Mr. Fraser: If your Honor please, at this time the plaintiff will make the general objection to the receiving in evidence of the exhibits described by Counsel for defendant, on the ground that these exhibits as to this defendant constitute hearsay; on the further ground that, with the exception of the report marked 1927, that material, in our opinion, is irrelevant because of their remoteness and, further, because they are prepared by somebody that is not an officer or associated with the [114] company.

Then I make the further objection to the receiving of these documents, on the ground that if they are being offered for the purpose of showing general intent on the part of the three parties involved in the transaction, which the evidence has conclusively established at this time that is the only pur-

(Testimony of William L. Brewster.)

pose that they could be received for, your Honor, would merely bear upon the intent of one party, Building Syndicate Co. They would not be any evidence, in the absence of further foundation, of intent of Lumbermens Trust Company or Union Trust Company.

The Court: Is there any question as to the authenticity of the reports?

Mr. Fraser: There is none, your Honor.

The Court: Did the reports come from the files of the plaintiff?

Mr. Fraser: They did.

The Court: They will be admitted.

(Thereupon, the photostatic copies of journal and ledger sheets above described and previously marked Defendant's Exhibits 52-A through 52-G, inclusive, were received in evidence.)

Q. (By Mr. Biggins): Mr. Brewster, during the recess have you had a chance to look at the pages in the books of the company's general ledger and journal which I have identified and that [115] have been admitted as Exhibits 54-A through -F?

A. Yes; I glanced at the pages.

Q. May I have these annual statements?

The Court: 52-A through -G.

(Documents presented to Counsel.)

Q. Is it not true, Mr. Brewster, that on the books of Building Syndicate, as set forth in Ex-

(Testimony of William L. Brewster.)

hibits 54-A through 54-F, the complete ledger on the table, that the entire interest of the property purchased from Northwest Bank was listed as an asset of Building Syndicate as set forth in its books?

Mr. Fraser: I will object to that question, your Honor, on the ground that the record should speak for itself. It calls for a conclusion.

The Court: Let me have the question.

(Question read by the Reporter.)

The Court: The witness has stated that he knows something about it and he has had experience in it. On the other hand, I do not believe, since he is an adverse witness, that you would be entitled to his opinion on the matter; therefore, the objection is sustained. This would be in the nature of opinion evidence, I believe.

Q. (By Mr. Biggins): Looking at what has been introduced in evidence, Mr. Brewster, as 54-A, would you care to see the document if the Court permits you to step from the stand?

The Court: Yes, you may step down. Can't we remove those [116] pages and get them in evidence?

Mr. Biggins: I am afraid if I undertake to do it it will just create a mess.

The Court: All right.

Mr. Biggins: Examine 54.

(Witness inspects exhibit.)

Q. (By Mr. Biggins): You see after I read:

(Testimony of William L. Brewster.)

“Building Syndicate. Portland, Oregon. Proposed Depreciation and Amortization Entries. As of December 31, 1927. For American Bank Building”——

And now the crucial language:

——“Conforming to Conclusions and Instructions of Directors—at February 9, 1928, as Per Letter of Authorization by A. R. Watzek, President.”

Do you see that language, sir?

A. I do.

Q. In your search of the books and records and files of the corporation, have you been able to find a letter of Mr. Watzek dated February 9, 1928?

A. No.

Q. Do you have any doubts that, as custodian of the records of this company, that this document identified and admitted in evidence as 54-A does truly set forth the conclusions and instructions of the company’s president?

Mr. Fraser: May I ask a question? [117]

The Court: The objection is sustained.

Q. (By Mr. Biggins): Analyzing Exhibit 54-A, Mr. Brewster, does this document show that depreciation is and has been claimed on the total purchase price paid for the property?

Mr. Fraser: Before the witness answers the question, may I ask a question in aid of objection?

The Court: Yes; you may.

Mr. Fraser: Mr. Brewster, were you in any way associated with the Building Syndicate in 1927?

The Witness: No; only indirectly. I was an

(Testimony of William L. Brewster.)

employee of Strong & MacNaughton Trust Company, which firm was employed to manage the building. They would rent the space.

Mr. Fraser: Did you have anything whatsoever to do with the transaction that we are discussing in court today?

The Witness: Not at all; not at that time.

Mr. Fraser: In view of that fact, your Honor, I would like to object to further inquiry from this witness, on the ground that any question that might be asked him pertaining to the placing of entries on any record might merely be his opinion.

The Court: Objection sustained.

Mr. Biggins: I will concede he is not a competent witness on that.

Q. You are familiar, I believe you said, with the annual accounting reports of three separate C.P.A.'s that have reviewed the books and records of this Building Syndicate? [118]

A. As I recall, I first saw those audits in 1932 when they were turned over to my employer, at that time Robert Strong, and when we assumed, Robert Strong and I as his employee assumed the management of the property, we signed a receipt to the Commonwealth Trust and Title Company at that time, and among other documents these audits were turned over to us. That's the first time I recall ever having seen—

Q. You do know as a matter of fact that all of these reports by three C.P.A.'s establish the total

(Testimony of William L. Brewster.)

purchase price as assets of the building; you know that? A. No; I would not.

Q. Do you know that they all set up the Land Certificates as liability of the company?

A. I—

Q. If you don't know, that is all right.

A. I don't know, no, as to that.

Q. Reading to you from one statement in the annual report prepared for 1930 by I. D. Wood & Company, I will read a statement, Mr. Brewster, and ask you if you know the facts, conversations or documents upon which this statement is based?

Mr. Fraser: Counsel, before you proceed, may I ask what year?

Mr. Biggins: Excuse me, I thought I said 1930. It is Exhibit 52-D, Page 4.

Mr. Fraser: Your Honor, may I make an objection at this [119] time on the ground of relevancy, competency and materiality, for the principal reason that matters and things transpiring after 1927 and possibly the first part of 1928 do not have a probative value with respect to the intention of the parties in 1927?

The Court: The objection is overruled.

Mr. Biggins: I am going to read a statement and then ask you a question, Mr. Brewster, from Page 4 of the annual report of the C.P.A. where it says:

“Land Trust Certificates, \$1,229,629.62—The title to the building site, the leasehold and the building is held in the name of these certificate holders.

(Testimony of William L. Brewster.)

1,350 certificates or indivisible shares of equitable ownership and beneficial interest in the above assets were issued and an amount of \$1,250,000 or \$925-.926 per certificate realized.”

Now, the crucial sentence, Mr. Brewster—this is under the Land Trust Certificates:

“These certificates in their intent represent an indebtedness of the corporation and not an evidence of ownership.”

Do you know of any documentary source in your custody of the books and records of the company that supports this statement or where it came from?

A. No. [120]

Mr. Biggins: That is all.

The Court: Do you have anything more, Mr. Stoel?

Mr. Stoel: Just one moment, your Honor. No; that is all, your Honor.

The Court: You may step down.

(Witness excused.)

Mr. Biggins: The Government rests, your Honor.

While they are discussing, if the Court please, I have made an offer to opposing counsel, if acceptable to this Court, that the Government has no objection to their examining the complete ledger at their leisure, sir, and inserting a page at any time. If the Court desires to keep the record open for that purpose, we have no objection.

The Court: 54-A through -G?

Mr. Biggins: -F, sir.

The Court: 54-A through -F. Have they been admitted?

The Clerk: You have admitted them, your Honor, but I had not marked them because they are still contained in the ledger account there.

The Court: Then we want to have those removed. Gentlemen, do you think there is anything in this particular book that you would want to use now?

Mr. Stoel: I think we would like the privilege of looking [121] through it, your Honor, before we close the record on that book.

Mr. Biggins: Very well; we have no objection on any addition of a document out of the book.

The Court: We will fix a time limit, then. You could do that some time during the latter part of this week, could you not?

Mr. Stoel: I am sure we could.

The Court: Then let us have the final closing, or if there is to be additional evidence on that additional point, say at 9:00 o'clock next Monday morning if we are to have additional evidence.

Mr. Stoel: That is satisfactory with me.

Mr. Biggins: I take it the testimonial evidence is closed now?

Mr. Stoel: We have not decided whether there is any rebuttal evidence, your Honor.

The Court: I think we should decide that, Mr. Stoel. I do not think we should decide this piecemeal. We have this one feature I think we should leave open.

Mr. Fraser: We are prepared to go ahead. We didn't want to create the inference we didn't want to make that decision right away.

The Court: Very well.

Mr. Biggins: We will have originals photostated and substituted for the originals. [122]

Mr. Stoel: Your Honor, we have no testimony of witnesses to offer in rebuttal. There have been marked here additional audit reports from the company's files as Defendant's Exhibits 52-H through -P, being the audit reports for the years 1934, '35, '36, '37, a second copy for the years 1937, 1938, 1939 and 1942, and we would like to have these a part of the record.

Mr. Biggins: We have no objection, your Honor. I was understanding the basis of objection was in far remoteness in time. That is why I confined the offer. If they want to withdraw their objection to remoteness in time, I will offer the whole bunch. I do not think they can cut both ways on that.

Mr. Fraser: Our purpose is that inasmuch as the other evidence was introduced, it is our position that these documents go to explain the intervening years. We would like to have you have the complete record.

Mr. Biggins: We have no objection.

The Court: That is -H through -P, 52.

Mr. Biggins: No objection, your Honor.

The Court: They will be admitted.

(Audit Reports above referred to for the years above referred to, previously marked

Plaintiff's Exhibits 52-H through 52-P for Identification, were thereupon received in evidence.)

The Court: Mr. Biggins, you will prepare a list of these [123] exhibits which will be attached to the pretrial order?

Mr. Biggins: It will be prepared today and given to the Court before leaving this afternoon.

Mr. Stoel: Your Honor, as additional evidence in rebuttal, we would like to enter the balance of the exhibits listed in the original pretrial order as it was filed here, and there are one or two errors in numbering here which I think we would like to straighten out, if I may.

The exhibits I am now offering are Supplemental Indenture of Lease listed in the pretrial order as No. 9, but it was mismarked No. 8.

The Court: That will be admitted as No. 9. We will mark it the same as in the pretrial order.

(The document above referred to, having been re-marked Plaintiff's Exhibit 9 for Identification, was thereupon received in evidence.)

Mr. Stoel: The next is Second Supplemental Indenture of Lease which is marked No. 9 but should be No. 10.

The Court: That will be entered as No. 10. Is there any objection to either of these? You have no objection?

Mr. Biggins: None at all.

The Court: They will be admitted.

(Document, Second Supplemental Indenture of Lease, having been re-marked [124] Plaintiff's Exhibit 10 for Identification, was thereupon received in evidence.)

Mr. Stoel: The remaining exhibits, your Honor, are Exhibit No. 15 in the pretrial order, being a printed letter from Building Syndicate to the holders of Land Trust Certificates, dated July, 1933, and Exhibit No. 16, a printed letter dated July 28th, 1938, the income bond of indenture between Building Syndicate and Portland Trust & Savings Bank, January 1, 1944.

That completes the plaintiff's case, your Honor.

Mr. Biggins: No objection.

The Court: They will be admitted.

(Documents above referred to, previously marked Plaintiff's Exhibits 15 and 16, respectively, for Identification, were thereupon received in evidence.)

The Court: Gentlemen, you have furnished rather complete trial briefs. You will have this other material that you may want to offer by next Monday. Do you feel that there is any necessity on the part of plaintiff of additional briefs?

Mr. Stoel: I think we would like to submit a brief since our trial memorandum was concerned primarily with the questions of property law rather than with the cases in the tax field, your Honor; whereas, the defendant's counsel, I think, was working primarily with income tax cases. I do not think the [125] two briefs are particularly—

The Court: Would you want to file a reply to the Government's brief?

Mr. Stoel: That would be satisfactory.

The Court: Then, in turn, if the Government has anything, you will have the privilege of replying to that, Mr. Biggins.

I do not want these facts to get away from me to the extent where I might have to secure a transcript, and I would like to ask that you have your answer in in ten days, Mr. Stoel.

Mr. Stoel: Thank you.

The Court: If you, in turn, Mr. Biggins, could get yours in—I realize the pressure that you are under, both of you gentlemen. Could you get it in within seven days after that time?

Mr. Biggins: I could put it in almost immediately, your Honor. If they could get a memorandum in, if I could suggest the 11th or 12th, I will work over the week end and have mine in by Monday, but then if I don't have it in by then, your Honor, I am in a whole week of jury trial.

Mr. Stoel: I think we can do that.

The Court: If you can do that, that will expedite the matter.

Mr. Stoel: Do you have any desire to have oral argument in this case, your Honor?

The Court: Of course, I can actually better decide that, [126] Gentlemen, after the briefs are in. I do not think so. I think that this is a case with the facts and the law actually in a field with which I have some familiarity, and I do not think, unless there are some particular points that the attorneys

feel that they could improve on by oral argument, I will ask for oral argument on it. After all, the briefs should cover those points. We will recess until 9:30 tomorrow morning.

(Trial concluded.) [127]

[Title of District Court and Cause.]

REPORTER'S CERTIFICATE

I, Gordon R. Griffiths, an Official Court Reporter to the United States District Court for the District of Oregon, do hereby certify that at the time and place mentioned in the caption I reported in shorthand all the testimony adduced and proceedings had in the above-entitled cause, that I thereafter caused my shorthand notes to be reduced to typewriting under my direction, and that the foregoing transcript, consisting of Pages 1 to 127, both inclusive, is a true and correct transcript of all testimony adduced and proceedings had in said cause, and of the whole thereof.

Witness my hand at Portland, Oregon, this 3rd day of August, 1960.

/s/ GORDON R. GRIFFITHS,
Court Reporter.

[Endorsed]: Filed August 5, 1960.

[Title of District Court and Cause.]

CERTIFICATE OF CLERK

United States of America,
District of Oregon—ss.

I, R. DeMott, Clerk of the United States District Court for the District of Oregon, do hereby certify that the foregoing documents consisting of Pretrial Order, Opinion, Findings of Fact, Judgment, Notice of Appeal, Bond for Costs on Appeal, Stipulation and Order extending time for docketing appeal, Designation of contents of record on appeal, Statement of Points, Stipulation and Order for transmittal of original exhibits, and Transcript of docket entries constitute the record on appeal from a judgment of said court in a cause therein numbered Civil 9887, in which Building Syndicate Co., an Oregon corporation, is plaintiff-appellant, and United States of America is defendant-appellee; that the said record has been prepared by me in accordance with the designation of contents of record on appeal filed by the appellants, and in accordance with the rules of this court.

I further certify that there is enclosed herewith reporter's transcript of testimony, dated November 4, 1959, filed in this office in this cause, together with all exhibits.

I further certify that the cost of filing the notice of appeal, \$5.00, has been paid by the appellant.

In Testimony Whereof I have hereunto set my hand and affixed the seal of said court in Portland, in said District, this 5th day of August, 1960.

[Seal] R. DeMOTT,
 Clerk;

By /s/ MILDRED SPARGO,
 Deputy Clerk.

[Endorsed]: No. 17037. United States Court of Appeals for the Ninth Circuit. Building Syndicate Company, an Oregon Corp., Appellant, vs. United States of America, Appellee. Transcript of Record. Appeal from the United States District Court for the District of Oregon.

Filed: August 8, 1960.

Docketed: August 11, 1960.

/s/ FRANK H. SCHMID,
Clerk of the United States Court of Appeals for the
Ninth Circuit.

